USDA

S. HRG. 98-615

NOMINATIONS OF SUSAN MEREDITH PHILLIPS, DANIEL OLIVER, AND WILLIAM E. SEALE

HEARING

BEFORE THE

COMMITTEE ON AGRICULTURE, NUTRITION, AND FORESTRY UNITED STATES SENATE

NINETY-EIGHTH CONGRESS

FIRST SESSION

ON

THE NOMINATIONS OF SUSAN MEREDITH PHILLIPS, OF IOWA, TO BE CHAIRMAN OF THE COMMODITY FUTURES TRADING COMMISSION; DANIEL OLIVER, OF CONNECTICUT, TO BE GENERAL COUNSEL OF THE DEPARTMENT OF AGRICULTURE; AND WILLIAM E. SEALE, OF VIRGINIA, TO BE A COMMISSIONER OF THE COMMODITY FUTURES TRADING COMMISSION

NOVEMBER 9, 1983

Printed for the use of the
Committee on Agriculture, Nutrition, and Forestry

U.S. GOVERNMENT PRINTING OFFICE

30-594 O WASHINGTON : 1984

S161-16

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NOMINATIONS OF SUSAN MEREDITH PHILLIPS, DANIEL OLIVER, AND WILLIAM E. SEALE

WEDNESDAY, NOVEMBER 9, 1983

U.S. SENATE,
COMMITTEE ON AGRICULTURE, NUTRITION, AND FORESTRY,
Washington, D.C.

The committee met, pursuant to notice, at 10 a.m., in room 328-A, Russell Senate Office Building, Hon. Jesse Helms (chairman of the committee) presiding.

Present: Senators Helms, Dole, Lugar, Jepsen, and Huddleston.

STATEMENT OF HON. JESSE HELMS, A U.S. SENATOR FROM NORTH CAROLINA

The CHAIRMAN. The Committee on Agriculture, Nutrition, and Forestry meets this morning, obviously, to consider the nominations of Dr. Susan Meredith Phillips to serve as Chairman of the Commodity Futures Trading Commission; Dr. William Seale to serve as a Commissioner; and the nomination of Mr. Dan Oliver to serve as General Counsel of the Department of Agriculture.

In the case of Susan and Dan, we are not welcoming new faces but, rather, are congratulating those already on the Reagan administration team who are moving up. While Bill Seale has not previously been associated with this administration, he is well known to many of the members of this committee because of his prior distinguished, dedicated, efficient service with and for Senator Huddleston.

Did I say that all right? [Laughter.]

Well, we were going to ask him to take half pay, you know.

Senator HUDDLESTON. Yes, retroactively.

The CHAIRMAN. Yes. [Laughter.]

Susan is no stranger to the members of this committee: She served as a Commissioner on the five-member CFTC since November of 1981.

During that time she has distinguished herself by working with both the other Commissioners and Members of Congress during the course of the Commission's reauthorization and by implementing many of the policies inaugurated as a result of that reauthorization.

In addition, Dr. Phillips has served as acting Chairman of the Commission since April of this year. Her thoughtful leadership has enabled the Commission to build on the exemplary regulatory record established under the leadership of former Chairman Phillip

Johnson and to break new ground in many areas, including the area of agricultural options.

Dr. Phillips' appointment as head of this important Federal regulatory agency is another in a series of appointments of women to positions of major responsibility in the Reagan administration. She joins the ranks of a large number of women who serve the administration with great distinction, because of their outstanding qualifications for the positions to which they have been appointed. Those who most readily come to mind are Supreme Court Justice Sandra Day O'Connor, Transportation Secretary Elizabeth Hanford Dole, a native of my own State, Health and Human Resources Secretary Margaret Heckler, United Nation's Ambassador Jeane Kirkpatrick, as well as Assistant Secretary of Agriculture Mary Jarratt. I commend you, Susan, upon joining this prominent group as Chairman of the Commodity Futures Trading Commission, and look forward to hearing from you further today.

We have two congressional witnesses and one public witness who wish to offer testimony with regard to Susan's nomination. Senator Charles Grassley and Congressman Cooper Evans, both of Iowa, will appear; as will Mr. Michael Unger, president of the North American Securities Administrators Association.

Our USDA nominee, Daniel Oliver, currently serves as General Counsel of the Department of Education. He is a graduate of Harvard University and Fordham Law School. Mr. Oliver has been engaged in both the private practice of law and the management of a business. Prior to accepting the appointment to his current position, Mr. Oliver served as president of Rincon Communications Corp. in New York and as executive editor of the National Review magazine. He has practiced law in New York for almost a decade—serving with two firms. This background will be of great benefit to him as he becomes the Department's chief legal officer and undertakes the management of approximately 235 lawyers in the Department's Office of General Counsel. We welcome you, Mr. Oliver.

Our last nominee, Dr. Bill Seale, has been nominated to serve as a Commissioner on the Commodity Futures Trading Commission. He holds a doctoral degree in agricultural economics from the University of Kentucky and has written extensively in that field. Prior to being nominated to this position, Bill served as a principal agricultural legislative aide to Senator "Dee" Huddleston and as vice president for government relations of the Commodity Exchange, Inc. in New York. This background will be of great benefit to Bill in formulating market oriented responses to the regulatory issues that will face the CFTC. We welcome you also, Bill.

Suffice it to say that we welcome all of you here.

Senator Huddleston.

STATEMENT OF HON. WALTER D. HUDDLESTON, A U.S. SENATOR FROM KENTUCKY

Senator HUDDLESTON. Thank you very much, Mr. Chairman.

I, too, will reserve most of my comments and questions for the record.[1]

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[1] See pp. 32–59 for written questions from Senator Huddleston and Ms. Phillip's answers thereto.

I would just say that we've had a continuing interest from the very beginning in the CFTC; we watched it being formed, watched its early days and the struggles it has had; and we maintain that interest in my office, and I think all the members of the committee do too.

So we are very happy to see the nominees here today. I think the President made a good selection when he named Susan Phillips to the Commission. And I think President Reagan has made a very good selection in elevating her to the position of Chairperson of that Commission.

What questions I have—we often use these opportunities to ask questions about various operations, problems or whatever as to the Commission—I will submit for her answers. They have no bearing on her qualifications to serve as Chairman of the CFTC.

At the proper time, of course, I will introduce Mr. Seale.

The CHAIRMAN. Thank you, Senator.

You did that in record time. I remember a little poem that went something like this: I like a finished speaker, I really, truly, do; I don't mean one who's polished, I mean one who's through. [Laughter.]

Senator Jepsen.

STATEMENT OF HON. ROGER W. JEPSEN, A U.S. SENATOR FROM IOWA

Senator JEPSEN. Thank you, Mr. Chairman.

In October of 1981 I appeared before this committee and had the pleasure of presenting a fellow Iowan for Commissioner of the Commodities Futures Trading Commission, Susan Meredith Phillips.

Today, 2 years later, I am back before you to present this same person to the committee, but this time around it's for the purpose of presenting her for the Chairman's position of the same Commission.

I view it as a promotion of sorts that is well deserved.

Many of you have had the opportunity to work with Susan and have come to know her through her tenure as Commissioner. I think we are all in agreement that she certainly has lived up to the expectations we had set for her in October of 1981.

There were those in the industry who had some reservations about Susan. I had none. Her sense of professionalism, commitment, and responsibility to the burgeoning futures industry, as well as her expansive knowledge and understanding of the economics and mechanics of futures trading, were and are impressive.

Her professional record reinforces my own personal conviction that she is an excellent nominee for the chairmanship of the agency.

Susan is currently on leave from the University of Iowa where she is a member of the finance department. After coming to the university in 1974, Susan Phillips served in several capacities, including the positions of assistant professor of the department of business administration, associate professor of the finance department, and associate vice president of finance and university services of the University of Iowa.

In addition, Susan has somehow managed to find time in her busy work schedule to publish over 20 research-comment articles and substantial contributions to four books, all in the area of higher finance.

This is neither Susan's first leave of absence from Iowa nor her first day in Washington. She was here once before, from 1976 to 1978 as a Brookings economic policy fellow, and a Securities and Exchange Commission economic fellow.

These experiences, in addition to her managerial skills and her impressive record of publications, have been and continue to be of substantial value to the Commission.

In summary, Mr. Chairman, Susan Phillips is an outstanding choice to head the Commission, someone who can bring expertise to an agency. Not only does she have the expertise needed as the agency oversees a changing, expanding industry, but she has the objectivity needed to assure that the markets have the benefit of an openminded regulatory agency and the ability to grow within a changing financial world.

Mr. Chairman, I strongly recommend the nominee.

The CHAIRMAN. And well you should.

The Chair will recognize the members as they have arrived.

Cooper Evans, we are delighted to have you, and I think I know why you are here; and it's a good mission.

STATEMENT OF HON. COOPER EVANS, A REPRESENTATIVE IN CONGRESS FROM THE THIRD DISTRICT OF IOWA

Mr. EVANS. Thank you, Mr. Chairman, and members of the committee.

I am very pleased to come before you today to join the Iowa Senators in presenting to you Susan Meredith Phillips, now a Commissioner of the CFTC, and to offer my personal endorsement and support for her nomination as Chairman of the Commission.

Dr. Phillips' extensive education and management experience well qualifies her as a candidate for the chairmanship.

For 9 years, Dr. Phillips was associated with the University of Iowa, in my district. There she served as a professor in the finance department and assisted in the university budgeting as associate vice president for finance and university services; and, additionally, as the Senator mentioned, she is widely published and is accepted as an expert in her field.

I do not believe this committee could find a more competent, well-versed nominee.

As the Commodity Futures Trading Commission approaches its second decade of existence, it is important that the agency be led by a strong manager, an imaginative regulator, and a well-informed communicator, who can assure public confidence in the agency and the industry it regulates.

This is of particular importance, Mr. Chairman, to this industry which is, I believe, little understood outside its perimeter.

This summer, Mr. Chairman, Acting Chairman Phillips demonstrated her ability to correct difficult market situations without disrupting those markets.

This was not a normal summer for the futures industry. First we saw the termination of all trading on one exchange. The CFTC moved quickly, sending assistance in the way of auditors, surveillance personnel and trading and market staff to that exchange to make sure that traders were protected against undue losses, and that contracts be settled in an orderly way.

Second, Mr. Chairman, during this summer the grain markets were highly volatile, responding to the Nation's drought and shrinking grain reserves. I was pleased with the Commission's thorough investigation and its continuous monitoring of the grain market.

I strongly believe that it was through Dr. Phillips' leadership and guidance that these particular market difficulties were overcome in an orderly manner and without a market emergency.

Commissioner Phillips, I praise you for the work that you have done and for the work that I know you will accomplish as Chairman.

As a Commissioner and as the Acting Chairman, Dr. Phillips has made it a priority to build good working relationships with the public, the Congress, the futures industry, and the Federal regulators to assure that the agency is well represented and responsive to the changing financial world.

As Acting Chairman of the Commission since May of this year, she has kept the agency working at full speed to assure that the provisions Congress mandated in the CFTC Act of 1982 are implemented swiftly.

Under her leadership the Commission has issued rules and regulations for registration of new categories of persons involved in the industry, instituted a series of service fees to recover for the taxpayer some of the costs of Government regulation; and proposed numerous changes to streamline and improve the functions of the CFTC.

Mr. Chairman, Susan Phillips has already been confirmed once by the Senate for the position of Commissioner; and so I commend the President on his wise choice, and highly recommend that the confirmation process be repeated to make Susan Phillips Chairman of the CFTC.

And I thank you, Mr. Chairman, for the opportunity to appear before the committee.

The CHAIRMAN. Thank you. Thank you for coming.

Senator Grassley.

STATEMENT OF HON. CHARLES E. GRASSLEY, A U.S. SENATOR FROM IOWA

Senator GRASSLEY. Senator Helms, and members of the committee:

It is difficult for me to outdo Senator Jepsen or Congressman Cooper Evans in regard to this nominee, whether I was first, or, in this case, hearing what they had to say about her qualifications.

I have a statement which I will put into the record regarding Dr. Phillips—or, Susan, as I have come to call her.[1] She has been re-

[1] See p. 25 for the prepared statement of Senator Grassley.

sponsive to those of us in Congress not only to our general philosophy that we have but also by her ability to work with the law. And that's important for an organization that's only been in existence for about 6 or 7 years.

More importantly on the many occasions when I pointed out my concerns, she has been responsive. And that is important—for her agency as an independent arm of the Government from both Congress and the executive branch.

We need people in there like her who are willing to respond to the direction and concerns of those of us in Congress who see the CFTC doing business in a quasi-legislative-administrative-judicial capacity, that we don't have the time or the constitutional authority to do; and so, hence, are setting up these independent agencies.

She has responded well in her 2 years' of experience that I have observed; and I support her confirmation as Chairman of the CFTC.

The CHAIRMAN. Thank you.

Senator Dole.

Senator DOLE. I am just passing through—is this the filing place for futures financial opinions? [Laughter.]

I know Bill very well, and I certainly highly recommend him. I was here when Susan was first confirmed, and I have known her through her work. Also, a friend of mine on the Commission speaks most highly of you and your great objectivity.

So I am happy to be here to indicate my support.

I assume these nominations will be reported out and confirmed before we adjourn next week?

The CHAIRMAN. That is the intent of the Chair, certainly if we can get the paperwork done and have some ad hoc meetings off the Senate floor—if they don't blow it up. [Laughter.]

Thank you.

Susan, I've just been sitting here thinking of the women who are playing such a prominent role in Washington today, including your own good self. And I've got to ring in my favorite North Carolinian who is playing such a prominent role in Washington, Elizabeth Hanford, who is in the Cabinet; and Margaret Heckler, Sandra Day O'Connor, and Mary Jarratt, Assistant Secretary of Agriculture.

But my staff always reprimands me a little bit about my being so informal at these meetings; but I don't see any point in being overly serious when we have a delightful set of circumstances as we do this morning with the kind of nominees we have.

But I do want to pay my respects to Bill Seale. He holds a doctoral degree in agricultural economics from the University of Kentucky; he's written extensively. As has been indicated, he worked with Senator Huddleston. He was vice president for government relations, Commodities Exchange, Inc., New York, for 4 years. That's bound to be useful to you, Bill.

Dan Oliver is a man I've long admired He currently serves as General Counsel for Department of Education. He's a graduate of Harvard University, and Fordham Law School. Mr. Oliver has been engaged in the private practice of law and in the management of a business prior to accepting the appointment to his current position; he served as president of the Rincon Communications Corp. of New York, and as executive editor of National Review magazine. He

practiced law in New York almost a decade and that background and experience will be of great benefit to him.

So what we have, I would say to the Senators, are three superlative nominees; and we welcome you.

Now, we have Michael Unger, the president of the North American Securities Administrators Association, if he will come forward?

Our welcome to him will be equally warm.

STATEMENT OF MICHAEL UNGER, PRESIDENT, NORTH AMERICAN SECURITIES ADMINISTRATORS ASSOCIATION

Mr. UNGER. Thank you, Mr. Chairman, members of the committee.

I am Michael Unger. I am president of the North American Securities Administrators Association, which is an association of State and Provincial securities administrators from the United States, Canada, and Mexico; we're charged with the responsibility, by our State legislatures, for administering and enforcing securities laws. The association works to protect investors and to insure that the securities markets operate with a minimum of abuse.

We are particularly pleased, Mr. Chairman, to have the opportunity to appear this morning, for the simple reason that what happens in Washington has a very direct impact back home.

And as regulators who do interface with the commodities industry—though we are primarily securities regulators—we get complaints from investors who may have trouble with those folks who are regulated or who should be regulated.

And in that regard we are quite pleased to be here this morning. I am pleased to be here this morning on behalf of my fellow administrators to support the nomination of Susan Phillips as Chairman of the CFTC.

As members of this committee know, the States securities administrators are actively involved in protecting investors from fraud in the commodities industry, and in that regard we have a continuing interest in cooperating with the Commission.

When we last appeared before this committee during the CFTC reauthorization hearing in 1982, we expressed our concerns about the relative roles of the agency and the States in protecting investors. There are still many problems, including the recent spectacular frauds in the gold bullion area.

But in the months that Commissioner Phillips has been Acting Chairman, and since the reauthorization hearings last year, major strides have been taken in cooperation between State securities regulators and the CFTC; and we are particularly pleased at those strides. There has been much greater sensitivity at the Commission to the concerns of the securities administrators, as well as the citizens back home in our States.

And we applaud Commissioner Phillips for that, since she has been the person leading the Commission during that period of time.

The CFTC is understaffed. It is probably never going to be the kind of agency, in terms of resources, that will be able to handle all of the problems, nor is the Securities and Exchange Commission, for that matter; and for that reason it is important that the Commission work very closely with the States.

We know that through the active cooperation of the Federal regulators, State officials, industry, and the public, we will be able to prevent fraud from undermining the commodities markets. That kind of cooperation depends very much on the leadership at the Commission, and particularly its Chairman. Based upon our experience with Susan—and I know her well enough to call her by her first name—we are optimistic and absolutely certain that she will provide that leadership.

For those reasons, Mr. Chairman, members of the committee, we urge the committee to recommend confirmation of Susan Phillips as CFTC Chairman.

The CHAIRMAN. Mr. Unger, we thank you very much.

Now, Madam Chairman, we will hear from you any statement you may wish to make.

STATEMENT OF HON. SUSAN MEREDITH PHILLIPS, CHAIRMAN-DESIGNATE, COMMODITY FUTURES TRADING COMMISSION

Dr. PHILLIPS. Thank you very much for the opportunity to appear before you today.[1]

I would like to express my appreciation, and that of my colleagues on the Commission for the help this committee has given to the CFTC and its regulatory program, and for support of our efforts to be a conscientious and responsive regulator of futures trading.

This committee has always understood and recognized the ever-increasing importance to the American economy of futures trading in the economic functioning of the country.

Futures trading has now spread to virtually all areas of agriculture and to some areas of the financial markets. Nevertheless the purpose and regulation of these markets is the same, the roots of the market remain in agriculture.

In 1 week I'll celebrate my second anniversary at the CFTC. During these years we've witnessed a remarkable amount of activity.

The Commission has approved 43 new futures contracts, approximately 1,000 rule proposals from regulatory organizations, and processed over 75,000 applications for registration.

Also during this period, the Commissioners and staff spent much time with you during Congress' consideration of our reauthorization.

The 13 months of intense scrutiny by Congress during the reauthorization forced us to reexamine and reevaluate nearly all aspects of our existing programs.

From this we have a clearer picture of the development of the industry and its relationship to our regulatory effort.

The Futures Trading Act of 1982 will prove to be a farsighted legislative initiative. It charts the course of this young agency as it assumes more of an oversight activity, while challenging the industry to refine and strengthen its own self-policing activities.

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[1] See pp. 25–32 for the prepared statement of Dr. Phillips with accompanying paper on the Commission fee structure, curriculum vitae, and a letter from David Martin, Director, Office of Government Ethics to Senator Helms concerning Dr. Phillips nomination. The financial disclosure report has been retained in the committee files.

I believe this challenge is already being met. The dialog with industry leaders and users of the futures markets has convinced me of the widespread commitment to effective self-regulation, both in a philosophical and practical manner.

Not only can self-regulation operate more quickly and efficiently than does regulation, but it also provides an opportunity to limit the growth of Federal intervention in the day-to-day operations of the industry, and the attendant growth of Federal expenditures.

For example, the National Futures Association has begun a rigorous program of registration and the exchanges are making great strides in refining and improving their individual self-regulatory programs.

Notwithstanding the substantial progress at this time, in our discussions with industry leaders, we have made clear to them that we at the Commission take our oversight responsibilities very seriously. We will continue to carefully scrutinize the industry's self-regulation.

We are also committed to efficient, vigorous, and efficient use of our surveillance and enforcement resources to assure the integrity of the market and the prevention of fraud.

Working as partners, Federal oversight and effective self-regulation should continue to provide protection for the futures markets and those who participate in them.

My observation of futures trading, even while at the university before becoming a Commissioner, has given me every reason to believe that the explosion in trading and new contracts we have seen recently may only be the early phase of profound changes in the industry—in its concepts, size, and market composition. The development of an agricultural options proposal under the able leadership of Commissioner Kalo Hineman, and the diversification and refinement of risk-shifting financial instruments were largely made possible by the Futures Trading Act of 1982. I am hopeful that both will give added impetus to innovation in the futures industry.

However, we all recognize that innovation, whether in international linkages, electronic trading, or third and fourth generation trading instruments, has resource implications for the CFTC. We must constantly reassess our own directions and efficiencies in light of these new developments and be willing to redirect our scarce resources where they can be most effectively spent.

Even in meeting this challenge, the Futures Trading Act of 1982 is farsighted. For example, the open season and information sharing provisions of the act give the Commission an opportunity to more fully involve the governments of the 50 States in the effort to provide a fraud-free marketplace. To this end we have begun an even more vigorous program of reaching out to the States, inviting them to take an active role in the protection of their citizens from those who mask their fraudulent activities behind a commodity theme. Emphasizing our commitment here, Commissioner Fowler West is taking an active and effective role as the representative of the Commission on our Advisory Committee on State Jurisdiction and Responsibility and in face-to-face dealings with State officials.

The maturation of the NFA and the increasing involvement of the States in enforcement matters will afford further opportunities

to redirect scarce Commission resources to address the changing shape of the futures markets.

The Futures Trading Act of 1982 contained a number of provisions which required responsive action by the Commission. I have prepared and distributed a longer statement which contains a brief report on the activities of the Commission to date in response to the 1982 legislation. With your permission, Mr. Chairman, I would like to ask that the statement be made a part of this hearing record.

The activities cataloged in that statement reflect a major part, but only a part, of the ongoing efforts of the Commission and its staff. In my 2 years' association with the staff of the CFTC, I have come to appreciate not only their unparalleled expertise but also their seemingly boundless enthusiasm and dedication.

Thank you once again for the privilege of appearing before you.

The CHAIRMAN. Thank you very much.

Senator Huddleston, would you please introduce Dr. Seale.

Senator HUDDLESTON. Mr. Chairman, I am pleased to present Dr. William E. Seale to the members of the committee. Bill is President Reagan's nominee to be a Commissioner of the Commodities Futures Trading Commission.

In fact, he needs little introduction to many of you—a majority of the members of the committee joined me in recommending to the President that Bill Seale be nominated to fill one of the vacancies on the Commission.

Bill has an admirable record of service to agriculture. He holds a master's degree and a Ph. D. in agricultural economics from the University of Kentucky, where he also served on the faculty.

During his tenure at the University of Kentucky, he managed the Ohio Valley farm analysis group—a subscription farm management program for commercial grain and livestock farmers—located in Henderson, Ky. Prior to his assignment to the Kentucky farm analysis program, Bill was county agriculture agent in Spencer County, Ky. While at the university, Bill authored numerous articles concerning Kentucky agriculture.

In January 1975, I convinced Bill that he could further his efforts to serve Kentucky agriculture by joining my staff here in Washington as my legislative assistant for agriculture and related matters. During his employment with the Senate, Bill worked with many of you and your staffs on issues that included farm commodity programs, agricultural transportation, soil conservation, crop insurance, livestock marketing, and commodity futures. Bill's assistance was invaluable to me during consideration of the Futures Trading Act of 1978.

In 1979, Bill joined Commodity Exchange, Inc., and served that organization as vice president for government relations until last spring. In that position, he deepened his knowledge of the futures industry.

Mr. Chairman, I am pleased that the President has accepted our recommendation that Bill be nominated as a Commissioner of the CFTC. I believe Bill Seale's broad knowledge and experience regarding agricultural and nonagricultural commodities give him qualifications that will be extremely useful to the Commission. Bill will bring to the Commission a valuable perspective on the rela-

tionship of farming, futures trading, and Government activities. And I know that he will provide to the CFTC the same professionalism and dedication that have been the hallmarks of his career.

Bill is married and the father of three children—two sons and a daughter.

I am proud to present him to you, and I urge you to join me in wholeheartedly supporting his nomination.

The CHAIRMAN. Thank you very much.

Bill, do you have a statement?

STATEMENT OF HON. WILLIAM E. SEALE, COMMISSIONER-DESIGNATE, COMMODITY FUTURES TRADING COMMISSION

Dr. SEALE. No, Mr. Chairman, I have no formal statement.[1]

However, I would like to say that the 4 years I spent working for the Senate, as Senator Huddleston's legislative assistant, working on matters within the jurisdiction of this committee, certainly were 4 of the most fulfilling years of my life. I will always be grateful to Senator Huddleston for convincing me to expand my horizons and venture beyond the walls of academia. And, Mr. Chairman, I am particularly appreciative of Senator Huddleston's friendship and counsel over the past 9 years.

I thank my other friends on this committee, especially Senator Leahy and Senator Cochran, for their friendship and guidance. And, Mr. Chairman, I want to thank you for your friendship over the years. It has meant a great deal to me.

I look forward to working with all of the Senators and staff of this committee regarding commodity futures matters.

The CHAIRMAN. Thank you, very much.

Mr. Oliver.

STATEMENT OF HON. DANIEL OLIVER, GENERAL COUNSEL-DESIGNATE, U.S. DEPARTMENT OF AGRICULTURE

Mr. OLIVER. Thank you, Mr. Chairman, for your very kind comments.

I would be happy to submit my statement for the record.

The CHAIRMAN. Very well, without objection it will be made a part of the record.[2]

Senator Lugar, any statement?

Senator LUGAR. Mr. Chairman, I would just like to move to the questions.

The CHAIRMAN. All right, very well.

I am obliged to ask the following questions of each of you:

If you are confirmed by the Senate, will you faithfully execute the laws passed by Congress, regardless of any previous statements you may have made, or bias you may have had?

Dr. PHILLIPS. Yes, sir.

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[1] See pp. 59–61 for the biographical résumé of Dr. Seale and a letter dated November 7, 1983, from David H. Martin, Director, Office of Government Ethics, to Senator Helms; the financial disclosure report of Dr. Seale has been retained in the committee files.

[2] See pp. 61–66 for the prepared statement of Mr. Oliver with accompanying biography, letter of November 7, 1983, to Senator Helms from David H. Martin, Director, Office of Government Ethics concerning Mr. Oliver's nomination, letter from William Riley, Jr., director of personnel, USDA to Mr. Martin; letter of November 2, 1983, from Mr. Oliver to Mr. Martin with attachment.

Mr. OLIVER. Yes, sir.

Dr. SEALE. Yes, sir.

The CHAIRMAN. Let the record show all answered in the affirmative.

If your nomination is approved and voted out of this committee, and confirmed by the Senate, do you promise to respond to requests and to appear and testify before this committee and any other duly constituted committee of the Senate?

Dr. PHILLIPS. Yes, sir.

Mr. OLIVER. Yes, sir.

Dr. SEALE. Yes, sir.

The CHAIRMAN. Let the record show all three answered those questions in the affirmative.

Dr. Phillips, I have been conducting drug hearings for several months now. Just about every financial instrument known to man is figuring in to the laundering of money and that sort of thing.

Have you any evidence that futures are being used by any element of the drug trade?

Dr. PHILLIPS. No, sir, we have not in our investigations had any of that brought to our attention; but we certainly would be on the lookout for it.

The CHAIRMAN. I hope you would monitor it, because the drug trade now exceeds—by a conservative estimate—$80 billion a year; and we want to make sure that that does not enter the futures markets.

There has been a lot of interest lately in the cash sales of certain precious metal dealers. Of course, I am referring specifically to the activities of the International Gold Bullion Exchange and the Bullion Reserves of North America.

Would you generally describe how these firms operate?

Dr. PHILLIPS. I'll try, sir.

It is my understanding that the two firms that you have mentioned essentially are dealers in the cash sales of gold bullion and coins or precious metals. This means customers put up their money, 100 percent of the money, at the time of purchase.

One or more of those firms stores the bullion, and sometimes a receipt is given to the customer. In some cases the firms purchase gold and store it.

In the cases you mentioned, unfortunately, there had not been sufficient purchases of the gold by the firms to cover obligations to customers.

In the one case in which we had customer complaints, we determined our jurisdiction is quite questionable. But because we were concerned, we did turn our information over to relevant State authorities and relevant Federal agencies and offered our expertise to work with them in further investigations. And those investigations were pursued.

The CHAIRMAN. You don't have jurisdiction over the activity?

Dr. PHILLIPS. Not over cash transactions, no, sir.

We regulate futures, options, and leverage contracts, but not cash sales.

The CHAIRMAN. What kind of role do the States play in these activities?

Dr. PHILLIPS. Well, I think the States essentially are our first line of defense; we try to work in conjunction with them, and try to offer them our assistance.

They actually are the ones that are closest to the issue.

The CHAIRMAN. You anticipated my next question, about what you are doing to assist?

How responsive are the States?

Dr. PHILLIPS. I think the States—well, it's certainly not true of all the States—some of the States certainly have their resource problems, like everyone else.

In some cases they are very responsive and very active.

Some of the things we've done is to assist in the investigations, help train State investigators, file joint enforcement actions, and make information available to them at their request.

The CHAIRMAN. Let us talk about agricultural options and the regulation of the trading of agricultural options. Would you summarize what CFTC has done thus far?

Then, if you will, make some sort of projection as to when agricultural options will be made available to the public.

Dr. PHILLIPS. Agricultural options—largely due to the efforts of people at this table—are now permitted as a result of the 1982 reauthorization legislation.

Beginning in March, the Commission put out for comment a proposed rulemaking. We realized, as we put it out, that a lot of people did not understand options, weren't quite sure how they would work; and we were concerned that we would not get any formal comments.

Thus, under the leadership of Commissioner Hineman, we literally visited 10 cities around the country—went out to try to talk to the various agricultural groups and to find out what their concerns were.

We came to the conclusion we needed more input and so, during the summer, we set up an Agricultural Options Advisory Committee as an organized research group and had representatives of the agricultural groups sit on the committee.

I might add they have met three times. The members are not receiving any compensation for their participation nor recovery of expenses.

It proved to me there's a lot of interest in the proper development of this program.

They have through their conversations identified the areas of concern; they came to agreement in a number of cases; and all the areas they were able to come to a consensus on, we included their thoughts into the proposed regulations.

Those regulations were voted on by the Commission in early October and now are out for public comment.

The comment period should be finished in mid-December.

We will analyze the comments, write the final regulations, and send them over to Congress for 30 calendar days of continuous session of Congress as part of the program; and then we'll start accepting applications for designation.

I would anticipate the program will be launched in the fall of next year.

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The CHAIRMAN. It will take a tremendous educational program to get a lot of people involved in it who might want to be, but just don't know enough about it.

Well, I see another friendly face just came in here.

I understand you got a little old bill over there involving dairy that you're going to work on today.

Ed Madigan, the ranking member of the Agriculture Committee—and it's always a comfort to look across the table at a conference and see him sitting there, because we always agree on everything—don't we, Ed? [Laughter.]

STATEMENT OF HON. EDWARD R. MADIGAN, A REPRESENTATIVE IN CONGRESS FROM THE 21ST DISTRICT OF ILLINOIS

Mr. MADIGAN. Mr. Chairman, I'm kind of nervous this morning. I've already smoked four cigarettes, and I just want to say I'm doing my bit for North Carolina. [Laughter.]

The CHAIRMAN. I'll send over a little sign that Senator Huddleston and I had printed: "We thank you for smoking." [Laughter.]

We are glad to recognize you, sir.

Mr. MADIGAN. I am sorry to be an interrupting factor here.

The CHAIRMAN. Not at all.

Mr. MADIGAN. But the bill is on the floor and they have already started on it; I need to be over there, Mr. Chairman. So I do appreciate your recognizing me.

I have come by this morning to speak a word on behalf of Bill Seale, whom I've known since he was a member of the staff here in the Senate.

He is a very educated man, more importantly, he's a smart man—and I know that's not always the same thing.

I think the problem we face as Members of the House and Senate in dealing with the futures industry is that we need an industry that not only avoids impropriety, but we also need one that works to avoid the appearance of impropriety.

And I think Bill Seale as a member of this Commission will be a positive force in bringing that about, without creating problems for an industry that normally has to conduct itself in a robust manner.

He will be an asset to us in the work we have to do. He is a good man.

The CHAIRMAN. Bill, you like that statement? [Laughter.]

Dr. SEALE. Yes, Mr. Chairman.

The CHAIRMAN. He does not come under the category stated so often by a late friend of mine, a distinguished lawyer down in North Carolina, named Herbert S. Seawell, Jr. His father was chief justice in our State.

Chubb died about 2, 3 months ago, and he was the most sought after dinner speaker in our State, and he was wont to say from time to time when he noted some of the mental gymnastics of some in academia that "that fellow had more education than his intelligence can stand," you know. [Laughter.]

But Bill doesn't fall under that category; I agree with that, he is both educated and intelligent.

We thank you very much for coming over here.

Mr. MADIGAN. If I may just add one thing?

Mr. de la Garza asked me to speak a word in his behalf for both of these nominees, and I would like that in the record.

The CHAIRMAN. We welcome that; that is duly noted.

Mr. MADIGAN. Thank you very much.

The CHAIRMAN. Thank you.

Dr. Seale, will you outline for the record what your duties were when you served as vice president of Commodities Exchange, Inc.?

Dr. SEALE. Yes, Mr. Chairman, I'd be happy to.

I served as vice president of the exchange from May 4, 1979, to April 1, 1983. During that time period I managed a five-person staff and had at my disposal two law firms, one based in Washington, one based in New York.

We monitored and analyzed all legislative and regulatory activities that may have impacted on the exchange and the industry generally.

I represented the exchange to Federal legislative and regulatory bodies. I assisted in formulation of comprehensive strategies to deal with Government-related matters.

I developed and conducted an educational program in futures trading and assisted in exchange policy development regarding a wide variety of futures related matters.

The CHAIRMAN. What role, if any, did you play in the management or decisionmaking process of the exchange during the period June 1979 through December 1981?

Dr. SEALE. During that period, Mr. Chairman, I managed and operated the Government relations office based here in Washington, D.C.

If the question is bearing upon policy issues of Commodity Exchange, Inc., I had no responsibility for determination of policy during that period or any other period during my employment at the exchange. Policy at Comex is determined by the board of governors.

The CHAIRMAN. What role, if any, did you play in responding to investigative or discovery requests made by Federal agencies or private parties in connection with the so-called silver crisis?

Dr. SEALE. To my recollection, Mr. Chairman, none. That would have been provided through inside and outside counsel.

The CHAIRMAN. Do you have any continuing relationship with the exchange, such as receiving severance pay or the right to a pension?

Dr. SEALE. Mr. Chairman, I do not.

I received upon my resignation, severance pay. I have no rights of any kind to any type of pension. I have no continuing relationship with the exchange in any way at all.

The CHAIRMAN. So any pension plan they may have did not vest so far as you are concerned?

Dr. SEALE. The pension plan, Mr. Chairman, is an all-or-nothing vesting at the end of 5 years; and I did not have 5 years' service.

The CHAIRMAN. One final question:

A conflict of interest, or the appearance of a conflict of interest, could arise between your public duty as a Commissioner and the duty to your former employer, if you as a Commissioner, vote on matters of financial interest to the exchange that arose or were pending at any time during your period of employment with the

exchange, what steps—I guess it's an accountability question—what steps have you taken or will you take to avoid even the perception of a conflict of interest?

Dr. SEALE. Mr. Chairman, as outlined in my letter to you of November 7, in view of my prior position with the exchange, I intend to disqualify and recuse myself in any particular matter involving a specific party or parties before the Commission, including requests for a license, privilege or exemption, enforcement actions, and litigation where I participated in a personal or supervisory capacity, or where I gained confidential, nonpublic information relevant to the merits of the particular matter.

I will also disqualify and recuse myself on a case-by-case basis in any matter where, despite lack of any actual conflict of interest, an appearance of conflict of interest makes it appropriate for me to do so. In making such a determination I have agreed to consult and be guided by the advice of the CFTC's General Counsel in his capacity as Designated Agency Ethics Official.

As a general proposition, I do not intend to disqualify and recuse myself from rulemakings, general policy determinations, legislative proposals and responses, interagency dealings, or general administrative duties imposed upon me by law.

The CHAIRMAN. Without objection, at this point in the record I will insert the full terms of the letter Dr. Seale wrote to the committee, and responses to questions which I filed with him.

[The following was received by the committee:]

MCLEAN, VA., *November 7, 1983.*

Hon. JESSE A. HELMS,
Chairman, Committee on Agriculture, Nutrition, and Forestry,
U.S. Senate, Washington, D.C.

DEAR MR. CHAIRMAN: As you are aware, I tendered my resignation as Vice President for Government Relations with the Commodity Exchange, Inc. (Comex) on March 23, 1983, effective April 1, 1983. I have no continuing relationship with Comex.

In view of my prior position at Comex, I intend to disqualify and recuse my self from any particular matter involving a specific party or parties before the Commission including requests for a license, privilege or exemption, enforcement actions, and litigation where I participated in a personal or supervisory capacity, or where I gained confidential, nonpublic information relevant to the merits of the particular matter.

I will also disqualify and recuse myself on a case-by-case basis from any matter where, despite the lack of any actual conflict of interest, an appearance of a conflict of interest makes it appropriate to do so. In making such a determination, I have agreed to consult and be guided by the advice of the CFTC's General Counsel in his capacity as Designated Agency Ethics Official.

As a general proposition, I do not intend to disqualify and recuse myself from rulemakings, general policy determinations, legislative proposals and responses, inter-agency dealings or general administrative duties imposed upon me by law.

Sincerely,

WILLIAM E. SEALE.

MCLEAN, VA., *November 3, 1983.*

Hon. JESSE HELMS,
Chairman, Committee on Agriculture, Nutrition, and Forestry,
U.S. Senate, Washington, D.C.

DEAR MR. CHAIRMAN: Enclosed please find my answers to the questions posed in your November 1, 1983, letter. After consultation with your Agriculture Committee staff I have taken the liberty of not repeating the questions.

I am also enclosing the letter of CFTC General Counsel and Agency Ethics Official, Kenneth M. Raisler, to David H. Martin, Director of the Office of Government Ethics, the content of which deals with the real or apparent conflict of interest issue

resulting from my employment at Comex. I would be happy to meet with you to discuss any further questions you may have.

With best personal regards,

WILLIAM E. SEALE.

Enclosures.

(1) I have no "personal interest" in any matter before the CFTC. There are no major matters I am aware of other than the Commission's investigation of the 1979–1980 silver market in which I may have, directly or indirectly, a conflict of interest or the appearance of a conflict of interest.

In view of my employment at Comex I intend to, and have agreed to, disqualify myself from any particular matter involving a specific party or parties before the Commission, including requests for license, privilege or exemption, enforcement actions, and litigation where I may have participated in a personal or supervisory capacity, or where I may have gained confidential, nonpublic information relevant to the merits of the particular matter.

I further will disqualify and recuse myself on a case-by-case basis from any matter where, despite a lack of any actual conflict of interest, an appearance of a conflict of interest makes it appropriate for me to do so. In making such a determination, I have agreed to consult and be guided by the advice of the CFTC General Counsel in his capacity as Designated Agency Ethics Official.

As a general proposition I do not intend to disqualify and recuse myself from rulemakings, general policy determination, legislative proposals and responses, interagency dealings or general administrative duties imposed upon me by law.

(2) Mr. Chairman, as you are aware I hold a Ph.D. in Agricultural Economics from the University of Kentucky and served on the faculty there for several years. My academic publications along with my research, teaching, and non-academic career have demonstrated that I am a strong advocate of the unimpeded forces of free market supply and demand.

(3) In my judgment, the differences in the markets and the functions of those markets regulated by the SEC and the CFTC warrant the continued existence of two independent regulatory agencies. Further, I am uncertain that any empirical evidence exists demonstrating the need for, or the potential benefits from, merging the two agencies.

I am unable to comment regarding streamlining requirements for persons registered with both the CFTC and SEC because I am not fully familiar with the current registrant requirements and the present degree of cooperation between the agencies regarding registration.

(4) I am not familiar with the CFTC's proposed rules regarding leverage transactions; therefore, I have not developed a position on them. Moreover, I have not considered the question of which leverage contracts ought or ought not to be offered for sale. However, I would be guided in this matter by the legislative history of the issue and the intent of the House and Senate oversight committees.

Risk disclosure is one of the cornerstones of commodity futures regulation. Since the CFTC requires risk disclosure for futures contracts, I see no reason why there should not be risk disclosure for customers of leverage dealers.

I am not aware of any proposed CFTC rules regarding price unpredictability. However, I am familiar with the general risk disclosure regulations the CFTC has had in place for a number of years and am supportive of these regulations.

I have no particular opinion regarding the price volatility of gold and silver.

(5) It is my understanding that the Freedom of Information Act contains an exemption for investigatory records compiled for law enforcement purposes. I further understand this exemption applies to CFTC enforcement action investigations.

(6) I was employed by Comex from May 4, 1979 to April 1, 1983. From time to time during that period I participated in executive staff discussions and reports regarding new contract applications, rule changes, proposed regulations, contract amendments, etc. then pending before the Commission. I have no knowledge of the status of any matter in which I participated that may now be pending before the CFTC.

(7) I am not familiar with the scope and progress of the current CFTC investigation of the 1979–1980 silver market. I do not recall having any substantive discussions with members or staff of the CFTC, SEC, or any other governmental agency or committee regarding the ongoing investigation.

Because of my lack of knowledge regarding the scope and status of the current CFTC silver investigation and the possible need, if confirmed, to recuse myself from consideration of or involvement in aspects of that silver investigation—I believe it would be imprudent and possibly unethical for me to comment on the investigation.

I am aware that civil legal actions were filed against Comex as a result of the 1979–1980 silver crisis. I have no knowledge of the status of any of these actions nor am I involved in any of these actions.

With regard to my responsibilities as a Comex Vice President, I was never involved in the defense of Comex regarding any type of litigation. Comex policy is determined by the Board of Governors and the procedures implemented by Comex regarding the 1979–1980 silver market were the direct result of Board determined policy. From time to time as a result of the problems; in the 1979–1980 silver market, representatives of Comex appeared before various Senate and House Committees. In my capacity as Government Relations Vice President I did consult with and counsel the Comex President prior to his testimony, regarding the particular procedures followed by the various congressional committees.

The CHAIRMAN. Mr. Oliver, what do you envision your role to be as General Counsel in the Department of Agriculture?

Mr. OLIVER. Mr. Chairman, my role as General Counsel of the Department will be both as attorney, chief lawyer, to the Secretary and also as a manager of 120 lawyers and 150 support staff people.

As the lawyer, I will provide formal and informal counsel to the Secretary and others in the Department; and I will represent them at administrative proceedings. And in doing that, I will try to assess the parameters of the law within which the Secretary will make policy decisions.

And some times I guess a lawyer has to say no to something that his client wants to do. That's part of the role of a General Counsel.

In terms of managing the office, my prepared remarks indicate that the office has limited resources, although it has grown enormously in the last 5 years; the attorneys handle about 150 cases each today; and they handled about a third of that 5 years ago.

So one thing to be done there is to get us into the computer age as fast as we can. That is something my predecessor has already begun. I'll try to do that as well.

I hope that the time I spend in managing the office will not prelude me from the practice of law.

The CHAIRMAN. This committee has always had a close working relationship with the Department of Agriculture, particularly with the Office of General Counsel with the former counsel. Now that is a two-way street.

And just for the record, I hope I can count on the same cooperation under your leadership.

Mr. OLIVER. You certainly can, sir.

The CHAIRMAN. Senator Huddleston.

Senator HUDDLESTON. I would just ask that I be permitted to submit written questions to Dr. Phillips.[1]

And I again reiterate my support for these nominees, and also for Mr. Oliver.

Thank you very much.

The CHAIRMAN. Thank you very much.

Senator Lugar.

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[1] See pp. 32–59 for the questions from Senator Huddleston to Dr. Phillips and answers thereto.

STATEMENT OF HON. RICHARD G. LUGAR, A U.S. SENATOR FROM INDIANA

Senator LUGAR. Mr. Chairman, let me just say I am deeply pleased to have Dan Oliver and Bill Seale here; I have tremendous confidence in both of them.

Dr. Phillips, I'd like to ask you this question, if you would agree to answer after taking a look at the record?

Last year during the consideration of the CFTC and particularly in conference, one of the most difficult problems was first of all one not imposed by you, that is, contract sanctity, a clause that's a part of the legislation, and which was always threatened with veto but, finally, met with signature.

And there were two other items you addressed. A number of studies were commissioned and a lot of time was spent trying to tailor those studies and get them in the hands, in one case, of Federal Reserve Board, which played a lead role.

What will finally happen to those studies?

Sometimes we see these things, and they create a great furor, and then we lose sight of them.

You've got a quote in your report, but at what point are we likely to see these studies? And will they be distributed to all the members of the committee, all Members of Congress? Or what disposition will you make?

Dr. PHILLIPS. There are three studies—actually, I guess there are four. One of the four is a report to Congress on the progress of the National Futures Association. That report will be submitted to the Congress.

There is a study that we refer to as the large hedger study, and we are looking in particular at large hedging operations in the livestock market, and we're looking as a control, at some of the other markets.

That is a 2-year study, and the first part of that will be contained in our annual report, 1983 annual report; and we will submit that to Congress. So you'll be seeing that in two installments, the first installment very soon to come.

Our third study is a study of—it's variously called, but generally it is the implications of trading on nonpublic material information. That study has two major thrusts to it—legal thrust, and an economic thrust. The study will also be completed, I believe, in the fall of 1984 and will be submitted to Congress.

The fourth study, which is the largest study, is being led by the Federal Reserve Board. Participating in that study is the CFTC and SEC. They are actively cranking away at it. We are at this point gathering data. We have put out a call for specific kinds of information to look at who is in these markets and how they are using them which will involve a survey of the actual participants.

That report is anticipated also to be completed in the fall of 1984, and will be submitted to both the House and Senate committees.

Senator LUGAR. I appreciate that answer to my question, because of compromise with friends in the House it would not have been possible that these reports were going to be taken seriously; and I just envision some day coming together again with some of the

same folks; and it would be useful and in good faith to have these studies.

Dr. PHILLIPS. I think it will be a contribution to the understanding of the futures market, not just the financial markets.

Senator LUGAR. One further final question, Mr. Chairman, as to the relationship of the CFTC and other agencies.

One of the greatest controversies throughout this whole period was over user fees in one form or another. This is resolved in all sorts of ways, but how is it possible for any of us, that is, the Senators, the industry, or whatever, to try to get some focus on what sorts of revenues are being generated from any of the actions you've taken, just trying in good faith with all the parties who negotiated on this, how can you isolate out this information so we can tell what is happening?

Dr. PHILLIPS. First of all, I didn't come to Washington to add to the debt.

One of the things that we are doing in the Commission is reviewing various services that we perform, specific services; and we've tried to identify the costs associated with those services and implement fees accordingly. I'll be glad to submit for the record an estimate of how much is generated by those fees.

The largest service fee is the $10,000 contract fee. The fee is based upon estimates of how much time is spent by the staff on those contracts, and we do believe that is a fair fee.

But we'll continue to review this. We certainly do not want to see a fee that would hamper the innovation and development of new contracts. This fee does not hinder submissions by the smaller exchanges, as far as we can tell, of contract proposals.

[The following information was received by the committee:]

ESTIMATED FEE REVENUES—FISCAL YEAR 1984

As a result of the Futures Trading Act of 1982, the Commission has created and revised several fees for services provided by the Commission.

Section 237 of the Futures Trading Act of 1982 added Section 26(c) to the Commodity Exchange Act. Section 26(c) allows the Commission to charge fees, not to exceed actual costs for services it provides to the public.

Since the Futures Trading Act of 1982 became law on January 11, 1983, the Commission has promulgated a number of fee regulations. As of August 23, 1983, the Commission began charging a nonrefundable fee of $10,000 per application for contract market designations. The Commission expects to receive between 30 and 50 applications during fiscal year 1984, yielding $300,000 to $500,000 in fees to the U.S. Treasury. (Note that all fees are deposited to the Treasury rather than to the Commission itself.) The Commission will review this fee in October 1984 to ensure that it does not exceed the actual cost to the Commission of reviewing and designating contract markets.

The Commission also raised its registration fees to reflect the actual cost of registering firms and individuals involved in the commodity futures industry. Specifically, the fee is now $275 per year for futures commission merchants (FCM's), $50 for commodity pool operators (CPO's) and commodity trading advisors (CTA's), $25 for floor brokers (FB's) and $6 for principals. Associated persons of FCM's, CTA's, and CPO's will pay a fee of $35 for a perpetual registration, or when they change their firm affiliation. The Commission expects registration fees to result in $1,500,000 to $2,000,000 during fiscal year 1984. Fees for registration will no longer be paid to CFTC when the National Futures Association assumes responsibility for registration.

Fees for requests for Commission records (such as FOIA requests), fees for transcripts of Commission meetings and fees for Commission reports (such as Commitments of Traders report) were also revised during fiscal year 1983. The Commission

expects to collect approximately $35,000 in fees for these requests during fiscal year 1984.

The Commission has proposed raising certain fees for filing reparations complaints. In particular, it has been proposed that the fee for an arbitration-type proceeding be $25, for an adjudicatory proceeding $250, and for an appeal $50. Depending on whether the proposed fees become final, the point during the year when they become final, and the number of people opting for formal versus informal proceedings, reparations fees will yield between $85,000 and $140,000 during fiscal year 1984.

There are several other fees under consideration, such as fees for rule enforcement reviews and financial reviews of self-regulatory organizations, and fees for audits of firms which are not members of an exchange or the National Futures Association. These fees could, if approved, yield an additional $300,000 to $500,000.

The Commission's total fee revenues during fiscal year 1984 are expected to be between $2 and $3 million. Because NFA is expected to assume responsibility for registration by January 1985, the fees collected by the Commission in fiscal year 1985 will fall to approximately $1 million.

Applications for contract market designation: 30×$10,000=$300,000 or 50×$10,000=$500,000.

Registration:

FCM (500×$275)	$137,500
CTA (3,000×50)	150,000
CPO (1,500×50)	75,000
FB (6,000×25)	150,000
AP's (40,000×35)	1,400,000
Branch office (3,000×6)	18,000
Total	1,930,500

Requests for Commission records, reports and transcripts equals $35,000.

Filing fees—reparations complaints equals $85,000 (assumes March adoption of rules). Could be as high as $140,000 if most complainants opt for formal adjudication rather than short-form procedure.

Rule Enforcement and Financial Reviews equals $300,000 (not yet adopted).

Audits of Nonmember Firms—Originally estimated as $915,000 for all audits. However, because FA is expected to perform most audits, would probably be around $200,000 if proposed and adopted.

Total fees equals between $2 and $3 million.

Senator LUGAR. Thank you very much.

Mr. Chairman, I would just add, it is to your and Mr. Huddleston's enthusiasm for an industry that is overseen by our committee by these efforts, it is a vital one, it is a growing one; and it provides more jobs and income opportunity in our country all the time. And it is so important that it is done right, and the people who are involved are extremely conscientious, as well as the people in the industry and as well as in the Senate, realize that somebody is staying on top of this very complex business.

Because if it goes sour, it would be a shame for all the people who would be hurt; it involves the public trust.

And I think this is a very important hearing, with all the people here who we know and who we like—their responsibilities are enormous.

We must have a lot of confidence in you because you are doing it day by day in a very fast market.

The CHAIRMAN. If either of us defaults ir our responsibilities it is a tragedy.

One final question for Mr. Oliver, submitted by Senator Cochran. I shall read it.

Federal marketing order programs have been a major part of U.S. agricultural policy for the last 47 years. Marketing order programs have proven to be beneficial to both producers and consum-

ers; producers have benefited by being assured of an orderly marketing system which avoids wide swings in the availability of fresh fruit, vegetables, and tree nuts.

Consumers have benefited from the programs by being assured of high-quality supplies of produce at reasonable prices.

Despite the overwhelming success of the marketing order programs, some in this administration, particularly at OMB, have attempted to systematically destroy Federal marketing order programs. This has happened despite the explicit authority given to the Secretary of Agriculture to administer marketing order programs under the Agricultural Market Agreements Act of 1937.

To get down to the question raised by Senator Cochran:

As General Counsel, will you be supportive of Federal marketing order programs and of the Secretary's explicit authority to administer those programs?

Mr. OLIVER. Mr. Chairman, I will certainly support the Secretary in performance of his duties. I don't know much about marketing orders yet, and can't speak to them. In terms of the question you asked earlier yourself—will I support the programs of this country: I certainly will.

The CHAIRMAN. If you have further thoughts on the matter, submit them in writing, please.

Any other questions or comments by any Senator?

[No response.]

The CHAIRMAN. Any further comments the distinguished nominees would like to make?

[No response.]

The CHAIRMAN. That brings us to the end of the road.

There being no further business to come before the committee, we stand in recess.

[Whereupon, at 11:10 a.m., the committee adjourned, subject to call of the Chair.]

COMMITTEE MEETING

THURSDAY, NOVEMBER 10, 1983

U.S. SENATE,
COMMITTEE ON AGRICULTURE, NUTRITION, AND FORESTRY,
Washington, D.C.

The committee met, pursuant to notice, at 3:50 p.m., in room S-327, U.S. Capitol, Hon. Jesse Helms (chairman) presiding.

Present: Senators Helms, Dole, Lugar, Cochran, Boschwitz, Jepsen, Andrews, Wilson, Leahy, Melcher, Pryor, and Heflin.

The CHAIRMAN. The committee will come to order.

On Wednesday, November 9, the committee held a confirmation hearing on three Executive nominations: Susan M. Phillips, to be Chairman of the Commodity Futures Trading Commission; William E. Seale, to be a Commissioner of the CFTC; and Daniel Oliver, to be General Counsel, U.S. Department of Agriculture.

Do I hear a motion that the committee report these nominations?

VOICE. So move.

VOICE. Second.

The CHAIRMAN. All in favor say "aye."

[Chorus of "aye."]

The CHAIRMAN. Opposed?

[No response.]

The CHAIRMAN. Thank you very much. The meeting is adjourned.

[Whereupon, at 3:51 p.m., the committee adjourned, subject to call of the Chair.]

COMMITTEE NOTE: November 10, 1983.—The nominations of Ms. Phillips and Messrs. Seale and Oliver were reported to the Senate.

November 15, 1983.—The nominees were confirmed by the Senate.

APPENDIX

STATEMENT OF HON. CHARLES E. GRASSLEY, A U.S. SENATOR FROM IOWA

Mr. Chairman, Members of the Committee, once again I am very pleased to join my colleagues to say a few words of support for Dr. Susan Phillips who has been appointed by President Reagan to serve as Chairman to the Commodity Futures Trading Commission.

During her 1981 confirmation hearing for her appointment to the Commission, I expressed confidence in Dr. Phillip's capabilities in making a significant contribution to the operation of the CFTC. During the past two years of her service as Commissioner, she has proven her understanding of the commodity trading industry and has exhibited the necessary leadership qualities during the past few months as she assumed the responsibilities of Acting Chairman of the Commission.

Iowan's are proud of the accomplishments of Dr. Phillips and we are confident that she will continue her high standard of excellence in her continuing efforts as Chairman of the Commodity Futures Trading Commission. I stongly endorse Dr. Phillips for this important CFTC position and urges my coleagues on the Committee to act favorably upon her appointment. Thank you for your consideration.

STATEMENT OF HON. SUSAN M. PHILLIPS, CHAIRMAN-DESIGNATE, COMMODITY FUTURES TRADING COMMISSION

Thank you for this opportunity to appear before you. The other Commissioners at the CFTC and I greatly appreciate the interest this Committee has in the Commission and its regulatory program as well as the support you have lent to our efforts to be a conscientious and responsive regulator of futures trading as a growing segment of the American economy.

I was sworn in as a Commissioner on November 16, 1981, just in time to participate in the agency's reauthorization. By any measure, the reauthorization process was a successful one. The Futures Trading Act of 1982 should prove to be a farsighted legislative initiative which will set the course for the future development of this young agency. One example of this is the inclusion in the reauthorization legislation of the "CFTC/SEC Accord", which provided the springboard for the introduction of a new family of trading vehicles. These new instruments allow those who provide financial services to our economy to more fully derive the benefits of future trading—price basing and risk shifting—which have been available to members of the agriculture community for more than a century.

The pendency of this legislation and its enactment, also provided the stimulus for many new contract market designations. Since I have been a Commissioner, 43 new futures and options contracts have been approved for trading, 12 of these during the past six months since I have been Acting Chairman of the Commission.

The Futures Trading Act of 1982 also provides the basis for the further development of the self-regulatory concept which has undergirded the regulation of U.S. futures trading since its inception in 1922. Through this legislation, the Congress challenged the futures trading community to effectively police itself, both at the exchange and industrywide levels, thus allowing the CFTC to assume more of an oversight role.

It has only been ten months since the Futures Trading Act of 1982 became law. During this time the Commission has moved vigorously to implement its provisions. I would like to use this occasion to report on the progress of the Commission in this regard.

REGISTRATION OF INTRODUCING BROKERS AND ASSOCIATED PERSONS

On August 3, 1983, the Commission adopted rules to implement the Act's new provisions concerning four new categories of persons who must be registered with the Commission: introducing brokers and the associated persons of introducing brokers, commodity trading advisors and commodity pool operators. The new rules establish registration requirements and procedures for these new categories of registrants; prescribe minimum financial, reporting, and recordkeeping requirements for introducing brokers; create certain exemptions from registration; limit the ability of associated persons to be simultaneously associated with different sponsors and set forth a framework for participation in the Commission's option pilot program by introducing brokers. Approximately 500 firms, with more than 4,000 associated persons, have taken steps to become registered as introducing brokers to date.

On May 20, 1983, the Commission published notice of the effectiveness of new Section 4k(5) of the Act, which imposes liabilities on registrants who hire or otherwise employ persons as associated persons if the registrant knew or should have known of facts regarding the associated person which are statutory disqualifications from registration. This notice also informed registrants of the procedure for informing the Commission of such facts, in order to avoid the liability imposed by Section 4k(5).

REPARATIONS

On February 15, 1983, the Commission published an advance notice of proposed rulemaking concerning revisions in its reparations procedure designed to simplify and streamline the adjudication of claims.

On June 6, 1983, the Commission published in the Federal Register a notice of the availability of the proposal, in which the Commission also invited "comment on the rules as proposed and suggestions for any other changes that would improve and expedite the reparations procedure." Commission staff currently is studying comments received in response to the proposed rules.

Because final rules had not been adopted on May 11, 1983, the effective date of the 1982 amendments to Section 14 of the Act, on May 16, 1983, the Commission promulgated interim rules to reflect certain of the 1982 amendments to Section 14 of the Act. In addition, a revision to Rule 12.1 clarified that the balance of the reparation rules would continue to apply until the Commission revised those rules with new rules of procedure pursuant to new Section 14(b) of the Act.

LEVERAGE

On June 23, 1983, the Commission published a notice making available proposed comprehensive rules on certain leverage transactions, in accordance with new Section 19(c) of the Act, which requires the Commission to regulate leverage contracts in gold or silver bullion or bulk coins or in any other commodities other than those specifically enumerated in the Act prior to the 1974 amendments. The Commission stated its intent to continue the current regulatory moratoria on the entry of new firms into the business of offering or selling leverage contracts in gold or silver bullion or bulk coins, platinum or copper. Commisson staff currently is studying comments received in response to the proposed rules.

Although the Commission is preparing to move forward with final rules, we received indications from the public comment process that the size of the potential universe of regulatees is greater than previously believed. As this Committee is aware, this regulatory approach is a major departure from the traditional oversight of self-regulation contemplated under the other provisions of the Act. Direct, "hands-on" regulation, without the intermediary of a self-regulatory organization is much more resource intensive than either exchange oversight or oversight over other industry self-regulators. Therefore, in order to avoid placing undue pressures on our already strained enforcement and regulatory resources, our present intention is to retain the moratoria on new entrants and products until the Commission gains knowledge and experience as to the numbers and types of individuals which may come under this regulatory scheme.

SERVICE FEES

In accordance with Congress' acknowledgment in amended Section 26 of the Commission's authority to promulgate a schedule of fees for its activities and functions, on August 23, 1983, the Commission adopted a nonrefundable $10,000 fee for contract market designation applications. The Commission stated that it would review the fee at the beginning of fiscal year 1985 and each subsequent year to ensure that

it reflects the actual costs of the designation process. In addition, exchanges were given an opportunity to withdraw pending applications and would not be required to pay fees on pending applications which were not withdrawn until the contract is designated or disapproved or until August 23, 1983. As a result of this action 29 of the 57 applications before the Commission were withdrawn.

On August 1, 1983, the Commission adopted revisions to its existing fee schedule to reflect the actual costs to the Commission of processing materials for registration and related materials. The revised fees are either the same or slightly higher than the fees then in effect. Since the Commission delegated responsibility for registering introducing brokers to the National Futures Association, the Commission did not adopt registration fees for introducing brokers or their associated persons. Also, on October 11, 1983, the Commission adopted a revised schedule of fees for requests for copies of Commission records, Commission reports, and transcripts of Commission meetings.

Commission staff currently is studying the feasibility of other fee schedules for specific regulatory services provided by the Commission. In the future, the Commission may consider promulgating fee schedules for Commission audits of firms which are not members of contract markets or of a registered futures association, in accordance with Congress' intent in amending Section 26.

STATUTORY DISQUALIFICATIONS FROM REGISTRATION

On October 25, 1983, the Commission voted to publish for comment proposed rules to implement the provisions of sections 8a(1)—8a(4) of the Act which authorize Commission to grant temporary licenses to qualified applicants for a period not to exceed six months and, in addition, establish a new system of statutory disqualifications enumerating the most important bases for finding applicants and registrants unfit for registration. These proposed rules would provide greater flexibility in the administration of the CFTC registration program and, thus, fulfill the intent of Congress that current registration procedures be streamlined and simplified "to enable the Commission to register fit persons more expeditiously and to remove unfit persons from the industry more promptly." The Commission expects to be able to adopt final rules in this regard early in 1984.

CONTRACT MARKETS

Commission staff has reviewed the Act's amendment concerning the designation process for stock index futures contracts and options and has determined that no revisions to Commission Guideline 1 are necessary at this time.

On January 28, 1983, the Commission adopted emergency interim regulations to govern the submission of contract market rules, pursuant to the new Section 5a(12) rule review procedures mandated by the Futures Trading Act of 1982. Specifically, the Commission revised its regulations to define "terms and conditions in contracts of sale" which must be submitted to the Commission for approval, amended Rule 1.41 to set forth those types of rules which are exempt from submission pursuant to Section 5a(12) of the Act, delegated to the Division of Trading and Markets the authority to determine when submissions which do not relate to "terms and conditions" do not require Commission review, delegated to the Division to authority to remit submissions which do not meet the form and content requirements set forth in Commission regulations and made certain other conforming amendments.

On October 18, 1983, the Commission adopted a staff recommendation on final rules which will put into effect Commission delegations and procedures pursuant to the new Section 5a(12) rule review procedures.

REGISTERED FUTURES ASSOCIATIONS

New Section 17(p) of the Act required the National Futures Association (NFA) to submit for Commission approval by April 11, 1983, rules that would require the Association to establish training standards and proficiency testing requirements, financial requirements and sales practice standards. To the extent the NFA had not obtained Commission approval of all such provisions covered by Section 17(p) prior to its enactment, the Association submitted the remaining rule changes needed to comply with Section 17(p), and the Commission approved those various submissions in April 1983. The National Futures Association is continuing to develop comprehensive programs to implement the rules required by Section 17(p), as mandated by new Section 17(q), which requires such programs to be in place by September 30, 1985.

On June 7, 1983, the Commission adopted a rule requiring all futures commission merchants which are required to be registered with the Commission to become members of a registered futures association, in accordance with Section 17(m).

On August 3, 1983, the Commission approved NFA rules under which the Association would administer registration functions on behalf of the Commission and authorized the National Futures Association to grant registration to applicants for registration as introducing brokers or associated persons of introducing brokers. The NFA has reported to the Commission that it anticipates assuming other categories of CFTC registration in early 1984, with completion of the transfer of registration responsibility by the end of 1984.

The Commission also approved rules governing disqualification from NFA membership which parallel the statutory disqualifications from Commission registration. In addition, the Commission has approved rules under which the National Futures Association may establish proficiency standards, including training, experience and proficiency testing to applicants for Commission registration through the National Futures Association. Subsequently, the Association submitted a requirement that persons applying for registration as associated persons of introducing brokers take and pass the National Commodity Futures Examination as a condition of registration.

Although the Commission has approved NFA rules governing conditional registration as well as denial, suspension, restriction or revocation of registration, the Commission has withheld delegating authority to act under these rules until Commission staff has developed a procedure for Commission review of these kinds of futures association registration decisions.

On May 17, 1983, the Commission revised Rule 170.8, regarding futures association arbitration, to reflect the statutory amendments which permit claims over $15,000, re-define the term customer and eliminate the restrictions on compulsory payment. Rule 170.8 also has been revised to include the requirement of new Section 17(b)(10) of the Act that a futures association must provide an "expeditious" procedure for settlement of customers' claims.

The Commission has appointed a staff liaison to the NFA who reports on a monthly basis to the Commission on NFA's progress in implementing its self-regulatory program. In addition, the staff and officials of NFA have reported to the Commission on its progress and plans in open sessions of the Commission in April and October of this year. Most notably, NFA has begun to implement auditing, registration, arbitration and testing programs.

SPECULATIVE LIMITS

An amendment to section 4a(5) of the Commodity Exchange Act gave the Commission authority to enforce exchange speculative limit rules in addition to any Federal speculative limit regulations. We intend primarily to use this authority to assist exchange rule enforcement efforts involving non-members, but this authority also enables the Commission to act independently of the exchanges to ensure that all speculative limit rules are enforced. Each exchange has submitted proposed rules setting speculative limits for approval by the Commission. Several sets have been implemented and we expect that we will be able to approve all remaining limits by early 1984. We also plan to review the current Federal speculative limit regulations for grain and soybean futures in fiscal year 1984.

OPTIONS

The 1982 amendments to the Commodity Exchange Act lifted the ban on the trading of agricultural options and authorized agricultural options transactions pursuant to a pilot program. In order to solicit the views of producers and agrbusinessmen on such a program, the CFTC scheduled a series of informational meetings around the country last March. In June, the Commission established the Agricultural Options Advisory Committee composed of representatives from farm (producer and middleman) and banking groups and the commodity industry to provide advice to the staff on developing the regulations to implement the new program. On October 4, the Commission published for public comment proposed rules governing an agricultural options pilot program. The next step will be for the Commission to review the comments received and thereupon determine whether to adopt final rules for submission to the Congress, in accordance with the provisions of Section 4c(c) of the Act. We anticipate that agricultural options may be trading by the fall of 1984.

CONFIDENTIALITY AND DISCLOSURE OF COMMISSION INFORMATION

On May 17, 1983, the Commission, in order to implement new Sections 8(e) and 8a(6), amended Part 140 of its rules to delegate to certain Commission officials the authority to disclose information under special circumstances to any department, agency or political subdivision of a state or foreign government, and to disclose information about disruptive or harmful market transactions to officials of registered futures associations or self-regulatory organizations. The Commission also added a new Rule 140.75, which delegates to the Division of Trading and Markets and certain Commission staff members the authority to transmit to any department of any state or political subdivision thereof the registration information required to be disclosed in new Section 8(g).

On May 25, 1983, the Commission proposed rules to implement Sections 8(a), 8(b), and 8(f) of the Act. The proposed rules would allow the Commission to withhold information contained in records of a pending investigation, to provide for notice prior to release of information pursuant to a subpoena for summons, and to delegate to certain Commission employees the authority to disclose information in connection with a receivership or bankruptcy proceeding. Commission staff is currently studying comments received on the proposal

PERSONNEL RESTRICTIONS AND PROHIBITIONS: CODE OF CONDUCT

The Commission has revised the Code of Conduct for Commission members and employees and former members and employees to conform to amended Section 9(d), which broadened the exceptions to the prohibition against investment transactions by Commission members and employees in actual commodities, and modified the procedure for notification of excepted investment transactions. In addition, the Commission extended the prohibition of Rule 140.735–9 to bar the dissemination of nonpublic information by members and employees about margin accounts, margin contracts, leverage accounts, leverage contracts and their functional equivalents consistent with amendments to Section 9(e) of the Act. The Commission also deleted all references to former Section 2(a)(7)(B), which contained essentially the same one-year post government employment restriction now contained in 18 U.S.C. section 207(c).

STATE JURISDICTION

The 1982 amendments significantly broadened the role of the states through the "open-season" provision which permits the application of any and all state laws to unlawful off-exchange transactions. Further, the states are now permitted under section 6d to enforce the antifraud provisions, of the Act in state courts as well as in Federal District courts. On October 19, the Commission adopted a rule which provides a procedure for states to notify the Commission of actions which they intend to bring pursuant to this section.

The Commission has worked very hard over the past year to encourage the states to take an active role in protecting their citizens from those who engage in unlawful conduct under a commodity theme. In this connection, the Commission's Advisory Committee on State Jurisdiction met in March to discuss the new provisions of the Act and the enhanced role of the states, and is planning to meet again in early 1984. A two-day seminar was recently conducted by CFTC enforcement staff at which representatives from 20 States were shown investigative and trial techniques for prosecuting commodity fraud cases. Finally, the Commission has informed every state attorney general and securities administrator that we stand ready to assist the states in developing and prosecuting off-exchange commodity fraud cases. This effort has resulted in five cooperative enforcement actions since January 1, 1983. We also have implemented new procedures for providing states with necessary registration information.

STUDIES

The 1982 amendments require the Commission to undertake a number of studies:

(a) Trading activities of large hedgers in the cattle, hog and pork belly markets—A detailed research plan has been developed and Commission staff have begun studying the extent of large hedger participation in the livestock futures markets through the analysis of daily market data, and interviews of selected large hedgers.

(b) Study of futures trading based on material non-public information—this study, also well underway, contains a legal and economic component as well as case studies.

(c) Special study of the effects on the economy of trading in futures and options—this study, led by the Federal Reserve Board, with participation by the CFTC and the SEC is proceeding well. The agencies are gathering information concerning the nature of participation in various markets and have prepared an initial outline. The study will also consider the basic economic functions and purposes of these instruments and their effects on the economy, including such issues as risk management, price stability and capital formation.

CONCLUDING COMMENTS

As an observer of futures trading for several years, even prior to my becoming associated with the CFTC, I have formed the opinion that the explosion of the regulated futures industry in the past few years may only be the early phase of profound changes in the industry—in its concepts, size, and market composition.

We at the Commission are prepared to meet the challenges these changes may present. The Futures Trading Act of 1982 provides additional tools which will enable the Commission to be responsive to an innovative industry through reliance on effective self-regulation with rigorous Commission oversight, and efficient "targeting" of problem areas.

CURRICULUM VITAE OF SUSAN M. PHILLIPS, SEPTEMBER 1983

Personal:

Date and place of birth: December 23, 1944; Richmond, Virginia.

Education:

1967—B.A. (Mathematics, Economics); Agnes Scott College.

1971—M.S. (Finance, Economics); Louisiana State University.

1973—Ph.D. (Finance; minors: Economics, Management); Louisiana State University (Dissertation: "The Portability Concept: Development, Growth and Future Direction"; State Farm Companies Foundation. Dissertation Grant).

Employment:

1967-1969—Research Assistant, later Research Technician in Group Pension.

Summer 1970—Actuarial and Research Department, John Hancock Mutual Life.

January 1971—Insurance Co., Boston, MA.

1973-1974—Assistant Professor, Finance Department, Louisiana State University.

1974-1978—Assistant Professor, Department of Business Administration, University of Iowa (on leave from June 1976 to July 1978).

July 1976-July 1978—Brookings Economic Policy Fellow (1976-77), SEC Economic Fellow (1977-78); Directorate of Economic and Policy Research, Securities and Exchange Commission.

April 1978—Present—Associate Professor, Finance Department, University of Iowa (on leave from November 1981 to present).

February 1979-November 1981—Associate Vice President of Finance and University Services, University of Iowa (Interim Assistant Vice President, February 1979-June 1980).

November 1981 to present—Commissioner, Commodity Futures Trading Commission, 2033 K Street, N.W., Suite 804, Washington, D.C. 20581 (Acting Chairman, May 1983 to present).

Professional affiliations and activities:

American Finance Association, Southern Risk and Insurance Association (Secretary/Treasurer, 1975-76; Second Vice President—Program Chairman, 1976-77; First Vice President, 1977-78; President, 1978-79).

Public testimony (other than related to job):

Expert Witness on Private Pension Portability Before the Subcommittee on Retirement Income and Employment of the Select Committee on Aging, U.S. House of Representatives, April 6, 1978.

Honors and awards:

Phi Beta Kappa, Beta Gamma Sigma, Agnes Scott College, April 1971; Chicago Board Options Exchange Pomerance Prize Award (Outstanding Research in Options), December 1980; Outstanding Alumna Award, Agnes Scott College, April 1982.

RESEARCH AND PUBLICATIONS

Publications:

1. "Viable and Safe Markets—The Role of the Commodity Futures Trading Commission", National Journal, September 3, 1983.
2. "CFTC's View of Financial Futures" World Financial Futures Conference Proceedings, Financial Times, London, September 1982.
3. "A Comparison of Margin Requirements for Options and Futures" with Paula A. Tosini, Financial Analysts Journal, November-December 1982.
4. "Exchange Listing and the Cost of Equity Capital" with J. Richard Zecher, U.S. Securities and Exchange Commission Capital Market Working Papers, No. 8, March 1982.
5. "A Comparison of Options and Futures in the Management of Portfolio Risk" with Eugene Moriarty and Paula Tosini, Financial Analysts Journal, Jan.-Feb. 1981.
6. "Trading Costs or Listed Options; The Implications for Market Efficiency" with Clifford W. Smith, Journal of Financial Economics 8 (1980).
7. "The Supreme Court's Decision on The Daniel's Case: Implications for Pension Regulation," Journal of Risk and Insurance, December 1979.
8. "The Cost of Funding Benefits Under the ERISA: A Statistical Survey—Comment: Authors' Reply," with Linda Pickthorne Fletcher, Journal of Risk and Insurance, March 1978; Second Reply, December 1979.
9. "The Future of the Portable Pension Concept," with Linda Pickthorne Fletcher, Industrial and Labor Relations Review, January 1977.
10. "The Cost of Funding Accrued Benefits Under the Employee Retirement Income Security Act of 1974: A Statistical Survey," with Linda Pickthorne Fletcher, The Journal of Risk and Insurance, December 1976.
11. "Potential Effects of Recent Pension Legislation," Best's Review, Life and Health Edition, March 1975.
12. "The Token Woman," with Linda Pickthorne Fletcher, Intercollegiate Case Clearing House (Harvard University), Case LCCH-#9475729. Reprinted in the following case tests: (1) Business and Society, eds., Hay, Gray and Gates; (2) Cases in Organizational Behavior, eds., White and Vroman; (3) Principles of Management in Organizational Behavior, Justin G. Longenecker; (4) Personnel and Human Resources Administration, Leon Megginson; and (5) Management, Justin G. Longenecker and Charles D. Pringle.
13. "The Finance Course: An Industry View—Comment," Journal of Financial Education, Fall 1974.

Books and book contributions:

1. "The SEC and the Public Interest," with J. Richard Zecher (MIT Press,, 1981).
2. "Deregulation of Fixed Commission Rates in the Securities Industry," with Dan Roberts and J. Richard Zecher, "The Deregulation of the Banking and Securities Industries," (Lexington Books, D.C. Heath and Company, 1979).
3. "Investment Environment, Analysis and Alternatives: A Book of Readings," Coedited with Richard A. Stevenson (West Publishing Company, 1977); and the following paper: "Yield-Risk Performance of Convertible Securities," with Robert M. Soldofsky and Richard A. Stevenson.
4. "Organizations: Theory and Behavior" by Herbert Hicks and C. Ray Gullett in Collaboration with Susan M. Phillips and William S. Slaughter, III; (McGraw Hill, 1975) and the following chapters: "Some Environmental Challenges," and "Decision Making."

Research results:

1. "An Analysis of the Market Structure for Dually Traded Options," with Dan Roberts, Midwest Finance Association, April 1979, Chicago, IL.
2. Comment on a paper entitled "Put-Call Parity and Market Efficiency" by Robert C. Klemkosky and Bruce G. Resnick, Southern Finance Association, November 1978 Washington, D.C.
3. "The Delta Factor—Implications for Risk Management, Market Making and the Monitoring of Credit Usage and Financial Stability," with J. Richard Zecher, U.S. Securities and Exchange Commission, June 1978, Washington, D.C.
4. "Effects of the Financial Structure of Assuming the Unfunded Accrued Liability as Imposed by the Employee Retirement Income Security Act of 1974—The Case of Major U.S. Firms," with Linda Pickthorne Fletcher, Financial Management Association, October 1977, Seattle.
5. "Analysis of Financial Data of Specialists' Operations," with J. Richard Zecher, Roger W. Spencer, Le Manh Tri, James P. Burgess and Jeffrey L. Davis, National

Market Advisory Board, Securities and Exchange Commission, November 15, 1976, Washington, D.C.

6. Comment on a paper entitled "The Effects of Taxes on the Cost of Equity Capital" by Timothy Nantell and Robert Carson, Midwest Finance Association, April 1976, St. Louis.

7. "Long Term Structure of the Secondary Equity Market," Financial Management Association, October 1975, Kansas City, Kansas.

8. "Affirmative Action in Recruiting Finance Faculty: Comments on the Supply Side," Colloquium Session on Affirmative Action in Recruiting at the Financial Management Asssociation meeting, October 1974, San Diego, CA.

OFFICE OF GOVERNMENT ETHICS,
OFFICE OF PERSONNEL MANAGEMENT,
Washington, D.C., October 13, 1983.

Hon. JESSE A. HELMS,
Chairman, Committee on Agriculture, Nutrition, and Forestry,
U.S. Senate, Washington, D.C.

DEAR MR. CHAIRMAN: In accordance with the Ethics in Government Act of 1978, I enclose a copy of the financial disclosure report filed by Susan M. Phillips, who has been nominated by President Reagan for the position of Chairman, Commodity Futures Trading Commission.[1]

We have reviewed the report and have also obtained advice from the Commodity Futures Trading Commission concerning any possible conflict in light of the Commission's functions and the nominee's proposed duties. Based thereon, we believe that Ms. Phillips is in compliance with applicable laws and regulations governing conflicts of interest.

Sincerely,

DAVID H. MARTIN, *Director.*

[Questions submitted by Senator Huddleston to Dr. Phillips and answers thereto:]

Question. What will be your goals for the CFTC, and what priorities will you set with respect to the work of the Commission, when you assume the Chairmanship?

Answer. Any regulatory program initiated by the CFTC over the next five years must take account of two primary factors: (i) the extremely vigorous growth of the futures industry, and (ii) the limited resources of the CFTC itself. As a result of these two factors, the CFTC must constantly strive toward efficiency in our regulatory approach, relying where appropriate on industry self-regulatory organizations, and focusing our energies on our paramount missions of protecting the integrity of the marketplace and protecting the small trader.

The development of the futures industry in recent years has been impressive. From 1975, when the CFTC was launched, through 1982, the volume of contracts traded on regulated American exchanges grew from 28.5 million to 107.6 million, and the number of registered futures industry professionals increased from 19,000 to 56,700. At the same time, the variety of trading instruments has come to include many new risk management instruments based on financial instruments, Eurodollars, petroleum, options-on-futures, and most recently stock market indices. In addition, CFTC's regulatory purview continues to cover such off-exchange instruments as leverage contracts and dealer options.

At the same time, the Commission staff has barely grown since 1977. (see attached chart)

There is every reason to believe that the futures industry will remain dynamic in coming years. This year, we have seen at least one exchange come forward requesting Commission approval for "linking" its trading with another exchange halfway around the globe. Exchange proposals are now pending before the Commission to trade instruments based on the consumer price index and other economic indicators.

To address this regulatory agenda, the CFTC will focus in coming years on coordinating our efforts both with industry self-regulatory organizations and other government agencies which share our concerns. As the still-new National Futures Association (NFA) develops in coming years, it will assume some of CFTC's current responsibilities of registration and auditing of firms. This movement of responsibility would allow the Commission itself to better focus its own resources on enforcement, market surveillance, and exchange oversight, as well as economic research on new contract proposals and to assure the continued utility of existing contracts.

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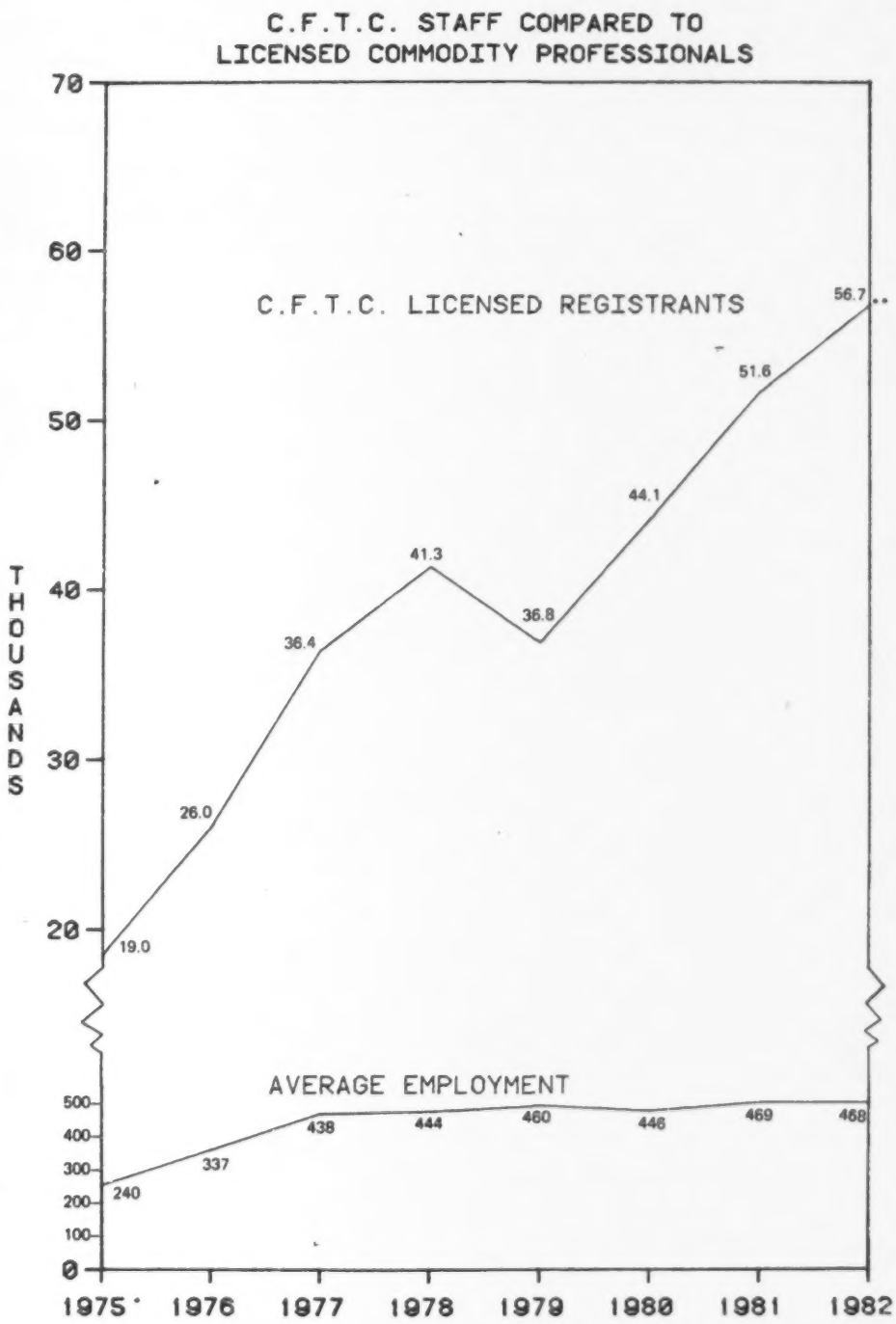
[1] The financial disclosure report has been retained in the committee files.

Similarly, the Commission will work to better involve State government law enforcement authorities in the investigation and prosecution of commodity frauds. The effort will be carried out not only through the CFTC's Advisory Committee on State Jurisdiction and Responsibility, but also through direct contracts with organizations such as the North American Securities Administrators Association and individual State officials through the Division of Enforcement.

Beyond these general themes, the CFTC will address a full platter of initiatives mandated by Congress in the Futures Trading Act of 1982, including several studies on different aspects of futures trading, and the development of regulations in different fields.

The Commission also will continually monitor and reassess our existing programs to assure that the benefits of such programs outweigh costs, and that the regulatory approach is economically sound and otherwise appropriate.



*CFTC began operations in April 1975. Figures for fiscal 1975 represent initial levels.
**As of July 31, 1982.

EXCHANGE-TRADED OPTIONS

Question. What is your assessment of the operation of the domestic exchange-traded option pilot program to date?

Answer. My assessment of the operation of the domestic exchange-traded option pilot program to date is that the program has been very successful from an operational and regulatory point of view. We have noted no problems in areas such as option expiration, exercise procedures, collection of premiums, or the clearing of trades. No sales practice problems have been reported in the pilot options program to date. The Commission's Complaints Section and the National Futures Association have received no formal customer complaints. The exchanges have reported no significant complaints. Such complaints that have been received have related to "technical" matters such as fills of option orders.

The National Futures Association and each exchange engaged in the pilot program are required to undertake an option sales practice audit program to monitor the marketing of exchange-traded options. As part of its oversight responsibility under the exchange-traded pilot program, the Commission has conducted reviews of those option sales practice audit programs. Each of the reviews of such programs conducted by the Commission's staff has found that the self-regulatory organizations have established and implemented effective option sales practice audit programs.

Question. Has the Commission seen any evidence of a recurrence of the customer abuses that prompted the option ban in 1978? In this connection, has the pilot program imposed special burdens on the Commission's enforcement resources?

Answer. The Commission has not seen any evidence of a recurrence of the customer abuses that prompted the option ban in 1978. The Commission's monitoring of the internal compliance programs of FCMs engaged in the offer and sale of options under the pilot program has indicated that those FCMs appear to have instituted supervisory procedures in accordance with the Commission's regulations. The Commission has also found that those FCMs appear to be complying with the additional disclosure requirements related to options. Potential abusive sales practices indicated by patterns of trading deep-out-of-the-money options, for example, have not been noted by the staff in reviewing the audit files of the exchanges and the National Futures Association, or in the staff's own spot check audits of FCMs. The Commission has also not seen any evidence that FCMs are bringing people into the option market who do not belong there, and in fact there have been cases where individuals have complained because FCMs have rejected potential option customers for failure to meet firm account acceptance criteria. Staff reviews have indicated that the vast majority of option traders, even those who do not fall within the "commercial" category, are sophisticated traders with prior experience in trading securities or futures or, in certain instances, the related cash commodity markets. The Commission also believes that the fact that the pilot program involves trading of options on regulated exchanges under the surveillance of exchange auditors has discouraged participation by questionable operators. All in all, these measures have resulted in the lack of customer complaints relating to exchange-traded option transactions, and there has been no substantial burden on the Commission's enforcement resources due to the exchange-traded option pilot program.

Question. Is the Commission seeing evidence of active commercial participation in these markets?

Answer. The Commission receives reports from the exchanges with respect to commercial participation in the option markets on a monthly basis. The exchanges derive the information contained in those reports from FCMs, which report to the exchanges which option positions are being held by commercials. The Commission's staff has reviewed those reports from the exchanges, and it appears that approximately one-third of the open interest in exchange-traded options is held by commercials. Also, as is the case with all Commission-designated futures or option contracts, there was substantial commercial participation in the development of the option contracts themselves.

Question. Do you feel the program should be expanded to permit an exchange to trade more than two options?

Answer. The Commission has recently proposed to permit exchanges to trade options on futures contracts involving two domestic agricultural commodities, in addition to the two options involving commodities other than domestic agricultural commodities which are permitted at the present time. An exchange could, therefore, be trading a total of four options if the agricultural options proposal is adopted. The Commission believes that this is an adequate and proper scope for the exchange-traded option pilot program at the present time, given the resources of the self-regulatory organizations and the Commission. The Commission will continue to monitor

the exchange-traded options pilot program and will recommend further expansion if conditions permit.

Question. How do you account for the limited interest shown by the exchanges in trading options on physicals?

Answer. I believe that the limited interest shown by the exchanges in trading options on physicals results from the fact that options on futures are instruments which are more familiar to the industry, as well as from the fact that trading of options on physicals would require more exchange resources for monitoring, especially with respect to the delivery process.

Question. In regard to agricultural options, do you see any special regulatory concerns with respect to those options that were not present with the other exchange-traded options that have been designated by the Commission?

Answer. The Commission has proceeded cautiously with respect to the issue of agricultural options. The Commission established an Advisory Committee under the outstanding leadership of Commissioner Kalo Hineman to examine all aspects of the issue. The Commission and the Advisory Committee have both been working toward the goal of permitting trading in agricultural options after a Congressional ban on such trading of approximately fifty years, and at the same time assuring that the abuses which led to that ban, as well as the 1978 option ban, do not recur.

Following a thorough examination of all aspects of this issue, the Commission proposed to allow exchanges to trade up to two options on futures contracts involving agricultural commodities. The Commission further proposed that, in line with the recommendation of the Conference Committee on the Futures Trading Act of 1982, the pilot program for agricultural options be "folded into" the existing option pilot program whenever possible, using the same kind of regulatory scheme already in place for the existing option pilot program. The Commission's experience is that the existing regulatory structure has worked well. Moreover, unless a need is specifically indicated, providing for different regulations to govern the trading of options on domestic agricultural commodity futures contracts and the trading of other types of option contracts would add unnecessary and duplicative regulations.

The Commission does anticipate, however, that agricultural options will be marketed to people in the agricultural sector of the economy who may be less familiar with futures and options trading than current traders in the existing pilot program. The Commission intends to emphasize the need to continue the present audit programs of the self-regulatory organizations to assure that abuses do not occur, and the Commission will continue its oversight program to achieve the same goal.

DEALER OPTIONS

Question. It has been five years since the "Grandfather" clause was adopted, and I'd like to know how it is working. Has the Commission had any regulatory problems with the sale of dealer options by grandfathered firms?

Answer. Only five firms currently are authorized to grant dealer options in this country: three domestic firms (Mocatta Metals Corporation, Dowex and Monex) and two wholly owned subsidiaries (Valeure White Weld S.A. and Continental Ore Europe, Ltd.) of a Swiss holding company that is owned by a major Swiss bank, Credit-Suisse, and First Boston, Inc., a domestic corporation having assets in excess of $200 million. The Commission has not encountered any regulatory problems with the granting and marketing of dealer options by these firms. The Commission believes that the strict standards established by Congress in section 4c(d) of the Act, as well as by the Commission in Commission rule 32.12, have substantially lessened the possibility that financially unsound or unscrupulous firms will sell options in a fraudulent manner.

These standards provide that grantors must (1) maintain a net worth of at least $5 million, (2) assume joint and several liability with any person that sells its options for all damages sustained by a purchaser of those options, (3) segregate daily "exclusively for the benefit of" option purchasers money equal to an amount by which the value of each transaction exceeds the amount received or to be received by the grantor for such transaction, (4) assign an identification number for each transaction, and (5) provide confirmation for all executed trades, including the execution price and transaction identification number. In addition, each grantor must maintain complete records concerning its dealer option transactions and make such reports available to the Commission.

The Commission's regulations prohibit dealer option grantors from directly selling their options to the public. As a result, dealer options are marketed only through futures commission merchants ("FCMs") registered as such with the Commission which are subject to stringent segregation, disclosure and recordkeeping require-

ments. Since grantors of dealer options are required by Commission rules to disclose the identity of all FCMs marketing their options, the Commission is able to identify such FCMs and to tailor the Commission's auditing of those firms accordingly. Moreover, since such FCMs are members of the National Futures Association ("NFA"), they also are subject to investigation and auditing by the NFA. As a result of these and other requirements, the Commission has been kept fully informed as to the identity of dealer option grantors and marketing FCMs and as to the scope of such activity.

Question. Has the Commission recently modified its interpretation of the scope of the "Grandfather" clause in permitting certain firms to sell dealer options in the United States? If so, how has the Commission's interpretation of the clause changed?

Answer. The Commission has not modified its interpretation of section 4c(d)(1) of the Act. Subsection (d) of section 4c of the Commodity Exchange Act authorizes the Commission to permit persons not domiciled in the United States to grant options under that subsection under such additional rules, regulations and orders as the Commission may adopt to provide protection to purchasers that are substantially equivalent to those applicable to grantors domiciled in the United States. The Commission first exercised such authority on March 19, 1979, when it waived the domicile requirement for Valeurs White Weld S.A., a wholly owned subsidiary of a Swiss holding company that is owned by a major Swiss Bank, Credit-Suisse, and a Delaware corporation, First Boston, Inc. The Commission conditioned its grant of such waiver, inter alia, on a requirement that First Boston, Inc. guarantee the performance when due of all obligations that Valeurs White Weld may owe to option customers in the United States pursuant to Valeurs gold option contracts or Commission rule 32.12 and that Valeurs submit to jurisdiction in the United States by appointment of a domestic agent for service of process.

On November 30, 1982, the Commission granted a similar request of Continental Ore Europe, Ltd. ("COE"), another wholly owned subsidiary of the same holding company that owns Valeurs White Weld, for waiver of the United States domicile requirement. As in the case of Valeurs White Weld, the Commission similarly required that First Boston, Inc. guarantee the performance of all obligations that COE may owe to option customers in the United States pursuant to COE silver option contracts or Commission rule 32.12 and that COE submit to jurisdiction in the United States by appointment of a domestic agent for service of process. The Commission's order with respect to COE was virtually identical in all material respect to the Commission's order concerning Valeurs White Weld.

The Commission notes that it consistently has narrowly construed the scope of section 4c(d) of the Act. For example, as a recent staff letter to COE makes clear, the Commission requires that, in order to be treated as a grandfathered firm by the Commission, a grantor on the grandfather date must have been (1) in the business both of granting options and of buying, selling, producing, or otherwise using the commodity on which the options are granted and (2) a bona fide commercial enterprise utilizing the commodity as opposed to a person who, for example, merely acquires small quantities of a commodity as a justification for owning commodities or merely engages in the retail buying and selling of a commodity or the possession of inventory for a speculative purpose. (A copy of this letter is attached.)

COMMODITY FUTURES TRADING COMMISSION,
DIVISION OF TRADING AND MARKETS,
Washington, D.C., September 26, 1983.

Re Continental Ore Europe

ARTHUR Z. GARDINER, Jr., Esq.,
Wilmer, Cutler & Pickering,
Washington, D.C.

DEAR MR. GARDINER: This is in response to letters dated April 18 and May 24, 1983, from Ms. Helen Torelli of your firm, and your letter dated August 26, 1983, concerning the proposed sale of silver options by Continental Ore Europe ("COE") pursuant to Commission Rule 32.12 and the Commission's Order ("Order") dated November 30, 1982.

As required by the Commission's Order, COE has provided the following documentation:

(1) An executed guarantee agreement meeting the requirements of paragraphs (a)–(c) of the Commission's Order whereby First Boston, Inc. ("First Boston") guarantees the performance when due of all obligations that COE may owe to option customers in the United States pursuant to COE option contracts or Commission Rule 32.12;

(2) Audited financial statements of First Boston;

(3) An opinion of counsel that the guarantee agreement is legally binding under the laws of the State of New York;

(4) A resolution adopted by First Boston authorizing and directing the First Boston board of directors to notify the Commission and COE if at any time First Boston's net worth falls below $100 million;

(5) Executed copies of the agency agreement, as amended on August 26, 1983, required by paragraphs 3 and 4 of the Commission's Order to the effect that First Boston will act as COE's agent to receive any requests for information authorized by the Commission's Order or by the Commodity Exchange Act and the regulations thereunder concerning COE's business; and

(6) Information concerning COE's silver business as required by paragraph 7 of the Commission's Order contained in: Affidavit and telex submissions from Robert Strebel on behalf of COE dated May 6, 1983, July 14, 1983 and August 17, 1983.

Moreover, as required by Commission Rule 32.12(a)(8), COE also has provided:

(7) The names of each person selling its options;

(8) An Affidavit of the Chief Executive Officer of COE containing representations that COE meets each and every requirement set forth in paragraph (a) of Commission Rule 32.12; and

(9) Recent financial statements certified by an independent C.P.A.[1]

The above-referenced filings are responsive to, and appear to satisfy, the applicable filing requirements of the Commission's Order and Commission Rule 31.12(a). Moreover, the information provided in the above-referenced documents appears to reflect activities that would qualify COE to grant options pursuant to section 4c(d) of the Commodity Exchange Act ("Act") and Commission Rule 31.12. The Division bases its opinion on all the information provided and, in particular, the representations made by Robert Strebel, Chief Executive Officer of COE, that (1) on May 1, 1978, COE was in the business of buying and selling physical silver and granting options on silver; (2) such transactions included, during the first four months of 1978, over 36 million ounces in spot silver sales and options granted on over 31 million ounces of silver; (3) such transactions have continued through the first quarter of 1983 (with 1982 spot silver sales of 158 million ounces and options granted on 33 million ounces of silver); (4) at least seventy-five percent of all such physical and option transactions were with commercial London bullion houses; and (5) sales of physical silver were effected by COE on the London Metals Exchange ("LME") as a principal for its own account and not as a broker.[2] Any different, changed, or omitted facts might require us to reach a different conclusion.

As you know, section 4c(d) of the Act provides an exemption from the general ban on options contained in section 4c(c) of the Act, for certain persons who . . .

"On May 1, 1978, [were] in the business of granting an option on a physical commodity and [were] in the business of buying, selling, producing, or otherwise using that commodity . . . ."

Since this provision was intended as a very limited exception to the general ban on options[3] and was understood as precluding a wholesale invitation to off-exchange options trading,[4] the Commission has strictly construed the scope of section 4c(d) of the Act and Commission Rule 32.12. Thus, the Commission has previously concluded that the requirement in section 4c(d) of the Act that a grantor be in the business both of granting options and of buying, selling, producing, or otherwise using the commodity on which the options are granted reflects a Congressional and Commission judgment that grantors must be bona fide commercial enterprises utilizing the commodity—as opposed to persons who, for example, merely acquire or

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[1] Commission Rule 32.12(a)(8)(iii) requires a grantor to submit its most recent annual financial statements certified by an independent C.P.A. Since COE could not meet the net worth requirement of Rule 32.12(a)(1), COE requested, and the Commission granted, a waiver of that requirement. Such waiver was premised upon an alternative arrangement whereby First Boston, Inc. would guarantee COE's obligations to purchasers located in the United States. Under such circumstances, the Division believes that the audited financial statements of First Boston submitted by COE provide the information intended by Commission Rule 31.12(a)(8)(iii).

[2] In his telex communication, Mr. Strebel essentially contends that brokerage activities on the IME satisfy the "in the business" requirement of Commission Rule 32.12. The Division does not agree that the mere execution of transactions on the IME satisfies Commission Rule 32.12, since such transactions could constitute de facto brokerage activities. The Division understands, however, that as of May 1, 1978 and thereafter, COE was in the business of buying and selling physical silver as a commercial principal with London bullion houses and that the transactions it effected did not constitute mere brokerage.

[3] S. Rep. No. 95-850, 95th Cong., 2d Sess. 24-25 (1978).

[4] *See* 124 Cong. Rec. S16530 (daily ed. Sept. 28, 1978) (remarks of Senator Huddleston concerning the Conference report on S.2391.)

own small quantities of a commodity and engage in isolated transactions in that physical commodity as a justification for granting options.[5] Similarly, in proposing amendments to the current Commission dealer option regulations, the Commission strictly construed the "in the business" requirement of section 4c(d) of the Act as excluding the retail buying and selling of a commodity, or the possession of inventory for a speculative purpose.[6]

Accordingly, the Division further premises its conclusion on its understanding, based solely on the information provided and the representations of COE's Chief Executive Officer, that the above-referenced silver transactions were effected by COE for bona fide commercial reasons other than for the purpose of qualifying to grant options on silver and did not constitute the retail buying and selling of silver or the possession of inventory solely for a speculative purpose.

The Division has not attempted to verify independently the information provided or the representations made by, or on behalf of, COE in the above-referenced documents. Therefore, this letter does not constitute a determination as to the validity of such information or representations. Moreover, the Division notes that Commission Rule 32.12 and the Commission's November 30, 1982 Order impose certain continuing obligations on COE and Its designated FCMs, as well as on First Boston, Inc. and the First Boston Corporation as the appointed agents of COE. Among the continuing obligations included in the Order is a requirement that COE (or its agents) provide the Commission with such additional information, as authorized by the Order or by the Commodity Exchange Act and the regulations thereunder, as the Commission may request concerning COE's business. (Pursuant to paragraph 3 of the Boston Corporation have agreed to serve as agents of COE upon which may be designated FCMs, or appointed agents do not satisfy the requirements set forth in section 4c(d) of the Commodity Exchange Act, Commission Rule 32.12 and the Commission's Order, the Commission may request further information, rescind its Order or take other appropriate action against COE as authorized by the Act.

If you have further questions concerning this matter, please call me at 254-8955.

Very truly yours,

ANDREA M. CORCORAN, *Director.*

Question. Has the Commission taken all steps necessary to make sure that firms claiming the right to grant options under the "Grandfather" clause fit within the narrow scope of that clause? That is, has the Commission verified that each such firm was, on May 1, 1978, engaged in the business of selling options in the United States and in the business of dealing in the underlying commodity with producers, processors, and commercial users of that commodity?

Answer. As required by Congress is section 4c(d)(1) of the Act, Commission regulations in effect on August 17, 1978, govern the granting of dealer options until the effective date of regulations issued by the Commission under section 4c(d)(2) of the Act. Pursuant to those regulations in effect on August 17, 1978, firms claiming the right to grant dealer options are required to (1) notify the Commission in writing of the name of each person selling its options and that it meets each and every requirement set forth in Commission rule 32.12(a), (2) provide evidence of compliance with each provision of Commission rule 32.12 by affidavit and (3) submit to the Commission its most recent annual financial statement certified by an independent public accountant in accordance with generally accepted accounting principles. Thus, the affidavit must establish, inter alia, that the firm was in the business both of granting options on a physical commodity on May 1, 1978 and of buying, selling, producing or otherwise utilizing that commodity. In this regard, the Commission has

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[5] *See* 43 Fed. Reg. 54220, 54222 (November 21, 1978). A contrary interpretation would render the general ban on options in section 4c(c) of the Act meaningless. Furthermore, the Division believes that the dual "in the business" requirement of section 4c(d) of the Act further reflects that the "commercial use" intended by that section must be something other than the mere purchase of a commodity solely for the purpose of writing options. *See*, generally letters from former Commission Chairman William T. Bagley to Representative Ed Jones, Chairman of the House Subcommittee on Conservation and Credit and to Senator Patrick J. Leahy, Chairman of the Senate Subcommittee on Agricultural Research and General Legislation, dated April 13 and March 30, 1978, respectively, reprinted in Extend Commodity Exchange Act: Hearings on H.R. 10284 Before the Subcommittee on Conservation and Credit of the House Committee on Agriculture, 95th Cong., 2d Sess. 650-651 (1978) (". . . the selling of options is a natural adjunct to their dealings in the underlying commodities . . ."; ". . . That is, a person who is not principally in the options business but rather in the business of dealing in the underlying commodities.")

[6] *See* 48 Fed. Reg. 23469, 23474 (April 27, 1981). While the Commission has not adopted those amendments, the language cited in the proposal accurately reflects the Commission's intent to construe strictly and narrowly the dealer option exemption of section 4c(d) of the Act.

required that the firm provide specific information with respect to the nature and scope of the firm's commercial and options business on May 1, 1978 and thereafter.

Although the Commission staff reviews the submitted documentation for compliance with the requirements of Commission rule 32.12, the Commission does not otherwise conduct an independent investigation or verification of the documentation submitted by a grantor unless we have reason to believe that the documentation provided is untrue.

Question. If the Commission has not done its own investigation with respect to the eligibility of firms claiming to be grandfathered, would the Commission now look at these firms to assure itself that they were indeed in both the physicals business and the options business on May 1, 1978, and that any representations they have made to the Commission about their activities on that date can be substantiated by records of option transactions, inventories of physical commodities, and transactions involving actual movement of physical commodities among producers, processors, and commercial users of those commodities?

Answer. As previously noted, Commission rule 32.12 does not contemplate that the Commission will investigate independently those firms which submit the required documentation. While the Commission's staff has, of course, reviewed the material submitted by firms for compliance with Commission rule 32.12, in particular evidence as to the nature and scope of the firm's commerical and options business on May 1, 1978 and thereafter, the Commission does not as a matter of practice, in the absence of any credible evidence to the contrary indicating non-compliance with the rule, or giving us cause for particular concern, initiate an administrative action or investigation of those firms. Should the Commission at any time learn of facts which indicate that a firm did not in fact qualify as a "dealer" under section 4c(d) of the Act, it would certainly institute an investigation. To date, however, the Commission has not received any complaints with respect to the activities of the relatively small number of firms granting dealer options in this country nor has it received any reports supported by credible evidence that any firm currently granting dealer options does not in fact qualify as a "dealer" under section 4c(d) of the Act.

Question. If a customer bought an option granted by a firm that claimed to be grandfathered but actually was not, would the customer have a right of recission to get his money back? Could he collect from the futures commission merchant that sold the option, or would he have to sue the grantor? Could he demand performance on the option if it was profitable, and rescission if it was not?

Answer. A customer who purchased an option granted by a firm that claimed to be grandfathered but actually was not presumably would have such equitable remedies as recission and monetary restitution. Such a purchaser could sue either the futures commission merchant that sold the option or the grantor of the option particularly in light of rule 31.12(b)(4) which makes both firms jointly and severally liable for performance of the option. It is unclear whether such a purchaser could demand performance on the option if it was profitable and recission if it was not. The Commission understands that the availability of such equitable remedies varies according to the factual context of each situation. However, since it generally is against public policy to enforce an illegal contract, we believe that once a firm were held to be operating illegally recission would ordinarily be an applicable remedy.

Question. What action would the Commission take if it found that a firm granting options under the grandfather clause was not eligible under that clause? Would the Commission take action against futures commission merchants that were selling the options as well as the firm that was granting them?

Answer. Section 4c(d) of the Act states that the Commission may terminate the right of any person to grant, offer, or sell options under that subsection after a hearing, including a finding that the continuation of such right is contrary to the public interest. Pending the completion of such termination proceedings, the Commission may suspend the right to grant, offer, or sell options of any person whose activities in the Commission's judgment present a substantial risk to the public interest. Such action may be warranted in the case of a firm that is granting dealer options but is not in fact eligible to do so under section 4c(d)(1) of the Act.

It is unlikely that the Commission would take punitive action against futures commission merchants that were selling dealer options of an ineligible grantor if such FCMs otherwise were in full compliance with the reporting, disclosure and segregation requirements of Commission regulations unless they knew or should have known that the evidence submitted by a grantor to the Commission was false. The Commission does not believe that such FCMs should be punished for the misrepresentations of a grantor.

Question. Several years ago the Commission proposed rules to permit firms which are not grandfathered to enter the dealer option business. When do you anticipate that final rules will be adopted?

Answer. In 1978, the Commission proposed regulations to implement section 4c(d)(2) of the Act. 43 Fed. Reg. 59396 (December 20, 1978). After reviewing the public comments on these proposals, as well as the staff's analysis of these comments, the Commission determined to republish that proposal for further public comment. 46 Fed. Reg. 23469 (April 27, 1981). The Commission determined to seek further comment because (1) substantial changes had been made by the Commission in a number of the prior proposals, (2) the Commission proposed language to implement proposals which previously were presented only as narrative requests for comment on particular issues and (3) certain additional amendments were then proposed for the first time. Id at 23470.

Further staff consideration of proposed rules to implement section 4c(d)(2) of the Act has been delayed because of the demand of higher priorities, including the Commission's reauthorization activities throughout 1982 and the promulgation of regulations to implement the amendments to the Act enacted at that time. Moreover, an exchange-traded options program has been initiated in the interim. The Commission anticipates that it may be able to allocate sufficient staff resources to conduct further rulemaking under section 4c(d)(2) of the Act later this fiscal year. However, as dealer options are principal transactions which require direct rather than oversight regulation, the Commission will have to assess carefully the sufficiency of its resources before implementing an expanded dealer options program.

LEVERAGE CONTRACTS

Question. The Commission recently proposed rules to provide for the regulation of leverage contracts. When does the Commission anticipate adopting final rules in this area?

Answer. On June 1, 1983, the Commission did determine to propose and solicit public comments upon comprehensive regulations governing the offer and sale of leverage contracts involving certain commodities. These regulations, which are being promulgated pursuant to the Commission's authority under Section 19(c) of the Act, would, among other things, include provisions concerning the definition of the term leverage contract, designation of leverage contracts to be offered and sold, the registration of firms and salespersons engaged in marketing leverage transactions, minimum financial requirements for leverage firms, requirements concerning the offset of leverage transactions, disclosure and segregation of customers' funds requirements, financial reports, recordkeeping and reporting requirements, and prohibitions concerning unlawful representations and guarantees against loss. The Commission intends to limit the marketing of leverage contracts pursuant to these regulations to those involving gold bullion or bulk coins, silver bullion or bulk coins, platinum or copper. The Commission also intends to continue in effect for a time its regulatory moratoria on the entry of new firms into the business of offering or selling leverage contracts. On June 23, 1983, the Commission published at 48 FR 28668 notice of availability of these proposed regulations which gave interested persons sixty days within which to submit written comments.

During this comment period and thereafter, the Commission has received fifty-four written comments from and on behalf of persons involved in a leverage business or wishing to enter such a business, and from others with an interest in the Commission's rulemaking. While the large majority of these comments generally supports the Commission's efforts to promulgate a comprehensive regulatory scheme for leverage transactions, many commentators additionally have suggested substantive modifications to the regulations as proposed by the Commission.

At the present time, the Commission's staff have analyzed the comments received, and are currently drafting final rules for adoption in the near future. It is anticipated that the Commission will be able to adopt these final rules in January 1984.

Question. Have there been any recent problems with regard to leverage transactions?

Answer. As a result of the comments it has received concerning its proposed regulations for leverage transactions, the Commission has become aware that a substantial number of persons and firms are interested in the leverage business. Specifically, the Commission has received comments from a number of firms of which it was unaware claiming to be lawfully marketing leverage contracts under the moratoria. In addition the Commission received numerous comments from or on behalf of persons or firms expressing an interest in engaging in a leverage business. As a result, and particularly with the eventual removal of the Commission's moratoria rules, it

can be expected that substantial and increasing Commission resources will need to be devoted in the coming years to the regulation of the offer and sale of leverage contracts.

Concerning current problems regarding leverage transactions, the Commission's Complaints Section has received numerous formal complaints seeking reparations during the previous two years from customers of four firms known to the Commission to be selling leverage contracts. These complaints, which were deemed by the Complaints Section to be sufficient to warrant their being forwarded to the firms and salespersons complained against for a response, were received against the following firms in the following numbers: First National Monetary Corporation, 94; Monex International Ltd., 90; Premex, Inc., 90; and International Precious Metals Corporation, 66.

The complaints received by the Commission against these four firms during the period of 1976 through October 1983 are also analyzed in the attached chart as a percentage of the total number of complaints received by the Commission. In addition to these formal complaints received against these four firms, the Commission has also recently been receiving complaints against an increasing number of persons and firms selling off-exchange instruments some of which may constitute leverage contracts.

Finally, you may be interested in the status of certain judicial and administrative proceedings involving leverage transactions that the Commission has initiated. In December 1982 the Commission filed an injunctive action against First National Monetary Corporation in the United States District Court for the Northern District of Illinois charging violations of the Commodity Exchange Act in connection with the offer and sale of certain contracts including precious metals leverage contracts marketed by the firm. Specifically, the Commission has charged, among other things, that the firm has engaged and is engaging in a deceptive and misleading sales campaign by falsely representing the nature, liquidity and profitability of these contracts. This suit has yet to be decided.

In December 1982, the Commission initiated an administrative lawsuit against International Precious Metals Corporation charging violations of the antifraud and supervision provisions of the Commodity Exchange Act and the Commission's regulations in connection with the firm's sale of leverage contracts in precious metals. Specifically, the Commission alleged, among other things, that from May 1979 through at least March 1980, the firm's account executives engaged in fraudulent sales practices in connection with the marketing of these leverage contracts. The sales practices included claims of nearly certain profits, statements which understated the risk of loss involved in the purchase of these contracts, failure to explain margin requirements, and failure to liquidate contracts in accordance with customer directives.

It was also alleged that from about January through March 1980, the firm was unable to service leverage customer accounts in a timely and accurate fashion and that it failed to take adequate steps to remedy deficiencies in its customer accounting system. This conduct, it was alleged, operated as a fraud or deceit upon customers in connection with the maintenance of their contracts and violated the firm's fiduciary responsibility to deal fairly and honestly with customers.

Additionally, the Commission alleged that the firm failed to supervise diligently the handling of commodity interest accounts carried by it for customers and failed to supervise diligently activities of its officers, employees or agents in violation of a Commission regulation requiring such supervision.

At the time it initiated the administrative proceeding, the Commission also accepted an offer of settlement which included a $200,000 civil monetary penalty from the firm. In addition, the firm consented to the entry of a Commission order without admitting or denying the Commission's allegations. The Commission's order accepting the firm's offer of settlement ordered the firm to cease and desist from violating antifraud provisions governing the offer, making and maintenance of leverage contracts sold by the firm and from failing to supervise diligently its personnel in connection with its leverage program.

In January 1978, the Commission instituted an injunctive action in the United States District Court for the Northern District of Illinois alleging that Premex, Inc., a registered futures commission merchant, and two of its principals were violating the Commission's minimum financial requirements applicable to futures commission merchants and were committing fraud in connection with the offer and sale to the public of leverage contracts involving precious metals in violation of the Commodity Exchange Act and the Commission's regulations thereunder. Subsequently, Premex and the other defendants in this action consented to the entry of a permanent injunction generally prohibiting them from engaging in unlawful conduct of

the type alleged by the Commission. Since the entry of that order of permanent injunction, the Commission has successfully moved before the District Court on two occasions to have the firm held in contempt for violating the order's proscriptions.

In a related administrative proceeding instituted by the Commission against Premex, an Administrative Law Judge has recently determined, among other things, that Premex and Samuel Zack, its president, violated the Act and the Commission's regulations by failing to meet the Commission's applicable minimum financial requirements and by fraudulently preparing and disseminating materially false and misleading promotional material in connection with the offer and sale of leverage contracts to the public. In his decision, which is currently on appeal to the Commission, the judge ordered that Mr. Zack pay a civil penalty of $250,000, that the registrations of Mr. Zack and Premex with the Commission be revoked, and that they be ordered to cease and desist from further violations of the Act or regulations.

COMPLAINTS AGAINST MONEX, PREMEX, FNMC, & IPMC

AS A PERCENTAGE OF THE TOTAL NUMBER OF

COMPLAINTS THE COMMISSION HAS RECEIVED

1976 - 1983

YEAR	COMPLAINTS TOTALS	RECEIVED NUMBER ON MONEX, PREMEX, IPMC, AND FNMC	PERCENTAGE
1976	160	2	1.25%
1977	350	3	0.86%
1978	873	2	0.23%
1979	903	29	3.2 %
1980	1401	170	12.13%
1981	1417	147	10.37%
1982	1079	92	8.53%
Oct. 1983	916	86	9.39%

STATE JURISDICTION

Question. The Commission's exclusive jurisdiction over commodities regulation has been repeatedly critized over the years, but has largely remained intact. The 1982 Act added an "open season" provision to encourage the states to participate more actively in the fight against off-exchange commodity scams. Do the states appear to be using the "open season" provision against off-exchange frauds?

Answer. Section 12(e) of the Commodity Exchange Act, 7 U.S.C. Section 16(e) (Off-Exchange and State Jurisdiction) the so-called "open season" provision, has been operative for a very short time. The Commission is disadvantaged in formulating an accurate answer to the question by virtue of Section 12(e)'s broad grant of authority which requires no notification of the filing of any action to the Commission. As a result, the Commission may not be aware of all the actions filed under Section 12(e) since January 11, 1983. The Commission is aware of one recent action filed by the

State of Hawaii entitled *Hawaii Office of Consumer Protection* v. *Nakomora & Assoc.*

Question. The Commission has taken steps to improve its coordination and cooperation with the states on the enforcement front. What further steps need to be taken in this area?

Answer. During the preceding year, the Commission has worked closely with several states seeking to remedy the sale of fraudulent, off-exchange contracts. In particular, the Commission has worked with California, Arizona, Colorado, Michigan, Texas, Florida and Iowa. In several of these coordinated efforts, joint lawsuits were filed by the Commission and individual states resulting in the protection of customer funds and imposition of cease and desist injunctive decrees.

During the upcoming year, the Commission will endeavor to continue its rather strong commitment in this area. For example, the Commission is in the process of establishing a state enforcement coordination unit in its Division of Enforcement. It is our expectation that this unit will be staffed to provide materials and advice to the several states for their use in combatting off-exchange fraud. This unit will also be able to direct the various state enforcement personnel to sister state agencies which may be investigating the same subjects and thus assist in a coordinated effort which the states may be unable to provide themselves.

The Commission will continue its already successful effort to encourage the filing of joint actions under Section 6d of the Act, 7 U.S.C. Section 13a-2. To date, the Commission has been involved in fifteen of these actions with eleven different states. While we expect this effort to continue, we anticipate a decline in the number of joint actions as the "open season" provision is utilized by more states.

In October of this year, the Commission conducted its second Annual State Cooperative Enforcement Seminar, which was attended by 35 participants from 20 states. A copy of the syllabus for that seminar is attached. The Commission is presently planning to conduct regional cooperative enforcement seminars during the upcoming year similar to the two-day session conducted in Washington, D.C. in October. The combination of cooperative enforcement seminars and the state enforcement coordination unit would greatly improve the already enhanced coordination between the Commission and the states.

SYLLABUS OF CFTC FALL SEMINAR FOR STATE ATTORNEYS GENERAL AND SECURITIES ADMINISTRATORS ON COOPERATIVE AND STATE ENFORCEMENT ACTIONS UNDER THE COMMODITY EXCHANGE ACT

OCTOBER 20-21, 1983, COMMODITY FUTURES TRADING COMMISSION, 2033 K STREET, N.W., WASHINGTON, D.C.

State Authority to Prosecute Fraud in Commodity Transactions

I. Method No. 1

A. Section 6d of the Commodity Exchange Act ("CEA") (7 U.S.C. section 13a-2)—1978 Amendments to CEA.

1. Creation of statutory standing for States to bring civil actions in federal district courts for violation on any provision of the CEA including any rule, regulation or order of the Commission thereunder.

a. Exceptions: State suits not permissible against contract markets, clearinghouses and floor brokers.

2. Explicit authorization for the States to obtain either injunctions, or damages, or both, or other further appropriate relief under the CEA.

3. A grant of jurisdiction to federal district courts to issue writs of mandamus to require defendants to take such action as is necessary to remove the danger of violation of the CEA or any Commission rule, regulation, or order thereunder.

4. Permitting, upon a proper showing, the granting without bond, of a permanent or temporary injunction or restraining order.

5. Providing expanded venue and nationwide service of process.

6. Permitting States to retain full powers under their own law to conduct investigations or to administer oaths or affirmations or to compel the attendance of witnesses or the production of documentary and other evidence.

7. Nothing contained in Section 6d shall prohibit an authorized state official from proceeding in State court on the basis of an alleged violation of any general civil or criminal antifraud statute of such state. (Section 6d(7))

B. How State Enforcement of the Commodity Exchange Act Works under 1978 Amendments to CEA.

1. Cause of action arises under Federal law, not State law.

2. Federal courts are the exclusive forum for these actions.

3. State action requires actual violations of CEA; accordingly, challenged investment vehicle must be subject to CFTC jurisdiction.

4. State required to forward copy of complaint to CFTC.

5. CFTC authorized to review complaint and intervene, but not required to do so.

a. Division of Enforcement personnel may be available to assist in the preparation and pursuit of any such contemplated action.

b. If desired, pleadings and legal memoranda filed in previous cases of similar nature will be made available.

c. To date, the Commission has filed 15 cooperative enforcement actions with 9 different states. (*See* Part C, infra.)

6. Advance notice desirable (but not necessary) in order to render assistance. (Section 12(a).)

7. Special customer protection provisions of Act especially appropriate for State actions.

a. Unlawful sale of off-exchange instruments.

b. Segregation of customer funds (17 C.F.R. sections 1.20–1.30, 32.6).

c. Disclosure of market risk in transactions (17 C.F.R. section 32.5).

d. Maintenance by FCMs of a minimum level of capital (17 C.F.R. section 1.17).

C. Joint Cooperative Enforcement Actions by the CFTC and the States in Prosecuting Fraud under 1978 Amendments to CEA.

1. Maryland: *State of Maryland and CFTC* v. *Annapolis Funding Co.*, C.A. No. H–80–1723 (D. Md. 1980).

2. New York: *State of New York and CFTC* v. *Commercial Petrolera Internacional, S.A.*, C.A. No. 80–Civ.–0689 (S.D.N.Y. 1980);

CFTC and the State of New York v. *Multi-National Holding Corp.*, C.A. No. 82–2173 (S.D.N.Y. 1982).

CFTC and the State of New York v. *Harold Sorkin, et al.*, 82–Civ–8279 (S.D.N.Y. 1982).

3. Georgia: *State of Georgia and CFTC* v. *Sterling Capital Co.*, C.A. No. 80–C–835A (D. Ga. 1980).

4. Texas: *State of Texas and CFTC* v. *International Bullion Clearing Corp.*, C.A. No. SA–81–CA–12 (W.D. Texas 1981).

5. Massachusetts: *CFTC and the Commonwealth of Massachusetts* v. *Norwell Trade Winds, Ltd.*, C.A. No. 81–1749 (D. Mass. 1981).

6. Ohio: *CFTC and the State of Ohio* v. *Troyer and Commodity Concepts Managed Commodity Fund*, C.A. No. 82–1931–A (N.D. Ohio 1982).

7. Missouri: *CFTC and the State of Missouri* v. *Thomas D. Morse, et al.*, C.A. No. 82–0312–C(3) (E.D. Mo. 1983).

8. Michigan: *CFTC and the State of Michigan* v. *Barbara A. Skorupskas, et al.*, C.A. No. 83–CV–1885 (E.D. Mich. 1983).

9. Illinois: *CFTC and the State of Illinois* v. *William A. Slavicek, et al.*, C.A. No. 83–C–4994 (N.D. Ill. 1983);

CFTC and the State of Illinois v. *Howard J. McConnell, et al.*, 83–C–5141 (N.D. Ill. 1983);

CFTC and the State of Illinois v. *George Ehrenberg*, C.A. No. 82–C–4925 (N.D. Ill. 1982);

CFTC and the State of Illinois v. *Financial Partners Brokerage, Ltd., et al.*, C.A. No. 82–C–5851 (N.D. Ill. 1982);

CFTC and the State of Illinois v. *Heritage Capital Advisory Services, Ltd., et al.*, C.A. No. 82–C–5955 (N.D. Ill. 1982).

II. Method No. 2

A. State Retention of Authority to Enforce State General Fraud Statutes to Protect Citizens Against Unlawful Commodity Activity.

1. Expressly reseved in Section 6d(7).

2. Commodity fraud perpetrators can be prosecuted under general State criminal or civil anti-fraud laws.

3. Limitation: *State of Texas* v. *Monex International, Ltd.*, 527 S.W. 2d 804 (Tex. Cir. App. 1975); *Clayton Brokerage Co.* v. *Mouer*, 520 S.W. 2d 802 (Tex. Cir. App 1975). The *Monex* and *Clayton Brokerage Co.* cases both addressed whether the State of Texas, subsequent to the 1974 Commodity Exchange Act, may obtain an injunction against commodity option trading or the offer of leverage transactions by persons who do not comply with a state regulatory program. Since the states are now without power to impose registration or other regulatory obligations with respect to transactions that became subject to the exclusive jurisdiction of this Commission on April 21, 1975, the Supreme Court of Texas held in those cases that it had become

moot whether the State of Texas might previously have been entitled to compel compliance with such requirements.

III. Method No. 3

A. Recent Legislative Changes to Section 6d pursuant to the Futures Trading Act of 1982, Pub. L. 97-444.

1. Encouragement of State Enforcement Actions:

a. State Antifraud Jurisdiction:

(i) Section 6d, as amended by new subsection (8)(A), expressly authorizes State officials to bring an action in State court to enforce the CEA against any person registered thereunder.

(ii) New subsection 8(B) of Section 6d requires the States to give prior written notice to the Commission before bringing such an action.

(iii) This same subsection (6d(8)(B)) authorizes the Commission to intervene in the State proceeding and further grants the Commission or the defendant the power to remove the case to Federal court.

(iv) The Commission may appear as amicus curiae in any State action

b. "Open Season" on off-exchange commodity fraud (Section 12(e)):

(i) Section 12(e) specifically authorizes all Federal, State and local officials to prosecute off-exchange commodity frauds under any relevant law or regulation.

(ii) Under this "open season" provision, State Attorneys General and Securities Administrators, for example, would be authorized to take action either in court or administratively against persons selling certain off-exchange commodity investments (i.e., diamonds, coal or strategic metals).

(iii) Section 12(e) explicitly permits the application of other Federal and State laws to activities and persons who unlawfully engage in commodity transactions outside the Act's regulatory structure (Sections 4c (options) and 19 (leverage) of the Act).

(iv) Likewise, such actions could be brought against any person engaged in an activity requiring registration or designation by the Commission who has not complied with those requirements.

(v) Activities which are subject to the comprehensive regulatory powers of the Commission and would remain within the Commission's exclusive jurisdiction include:

(a) Exchange-traded futures,

(b) Authorized commodity options programs, and

(c) Regulated leverage contracts.

c. Commission sharing of information with the States (Section 8(e)):

(i) The Commission is authorized to furnish to any department or agency of a State governement, upon request, any information obtained by the Commission and in its possession as a result of its administration of the CEA.

(ii) Information obtained by request to the Commission is to be deemed confidential, except that it may be used in a non-confidential manner in connection with an adjudicatory action or proceeding brough under either the CEA or state law and to which the state agency or department is a party.

(iii) The availability of the information should aid the States in preparing their own cases or enabling them to assess whether to join litigation being prepared by the Commission.

(iv) Thus, by making information sharing a two-way street, it is hoped that increased cooperation will result between the States and the Commission.

(v) Finally, under newly enacted Subsection 8(g), the Commission is authorized to furnish registration information to the States.

SUMMARY

To summarize, the three available avenues for an enforcement action by a State against an entity involved in commodity-like fraud are:

(1) An action in Federal court for violations of any provision of the CEA or Commission Regulations by a registered or unregistered entity, pursuant to Section 6d(1) of the Act, 7 U.S.C. Section 13a-2a, or an action in State court against a Commission registrant to enforce any antifraud provision of the CEA or Regulation thereunder pursuant to new Section 6d(8);

(2) An action in State court aganist a registered or unregistered entity for violations of any general civil or criminal antifraud statute of such State, pursuant to Section 6d(7) of the Act, 7 U.S.C. Section 13a-2 (7);

(3) An action in State court against an unregistered entitly to enforce any State statute, or rule or regulation thereunder, pursuant to new Section 12(e).

Question. One area with respect to which the Commission has exclusive jurisdiction is the regulation of commodity pools. Would you describe the Commission's regulatory scheme for commodity pools?

Answer. The Commission has in place a comprehensive regulatory scheme for commodity pools and commodity pool operators ("CPOs").

Unless exempt by regulation, CPOs and their associated persons must register with the Commission. This registration process includes conducting comprehensive fitness checks on these persons and on all individuals who are principals of CPOs.

Registered CPOs are subject to disclosure, reporting and recordkeeping requirements for the pools which they operate. These requirements are set forth in Part 4 of the Commission's regulations.

The disclosure requirements prescribe a Disclosure Document, which must be filed with the Commission prior to its distribution to potential clients, and which must include: the names and business backgrounds of the CPO, the pool's commodity trading advisor ("CTA"), and their principals; the actual past performance of these persons and the pool; complete descriptions of actual or potential conflicts of interests among the CPO, CTA, and carrying futures commission merchant, as well as all expenses of the pool; and a prescribed Risk Disclosure Statement which highlights the risks inherent in futures trading and participation in commodity pools. A CPO must receive a signed acknowledgment that a client has received a Disclosure Document before the CPO may accept any funds from the client.

The reporting requirements to pool participants include periodic Statements of Account and a certified Annual Report of financial condition, which also must be filed with the Commission. The recordkeeping requirements establish the records that must be made for pools and for CPOs' personal trading. These records must be kept for five years and must be available for inspection by the Commission and the Department of Justice.

Further, all CPOs are subject to advertising standards that prohibit the presentation of past performance in a false or misleading manner. In addition, CPOs must include a prescribed disclaimer of certain inherent limitations when presenting simulated or hypothetical performance results.

Question. Have the states sought to regulate commodity pools and, if so, what position has the Commission taken with regard to such regulation by the states?

Answer. States have made various attempts to register and regulate commodity pool operators. Most notable have been the Guidelines for Registration of Commodity Pool Programs proposed by the North American Securities Administrators Association ("NASAA"). The Commission has consistently taken the position that while states serve a vital role in the investigation and prosecution of commodity-related fraud and abuse, a role that was reemphasized and expanded by the Futures Trading Act of 1982, states remain preempted from imposing regulatory requirements on commodity pool operators, such as those requirements proposed in the NASAA guidelines.

Since 1974, when Congress created the Commission and granted it exclusive jurisdiction over the futures industry, Congress has made clear its preference for a single, uniform national regulatory scheme for the industry in order to avoid duplicative and potentially conflicting state and federal regulation. *See* S. Rep. No. 1194, 93 Cong., 2d Sess. 35–36 (1974). Congress made commodity pool regulation one aspect of the Commission's broad grant of authority when it determined that the activities of commodity pool operators "are affected with a national public interest" since these transactions "occur in such volume as to affect substantially transactions on contract markets." The 1974 legislation subjected commodity pools and commodity pool operators, for the first time, to the comprehensive regulatory scheme of the Commodity Exchange Act.

The legislative history of the Futures Trading Act of 1982 confirmed the Commission's pervasive jurisdiction over commodity pool activities. During its consideration of new Section 4m(2), 7 U.S.C. § 6m(2), which clarifies the extent to which the Federal securities laws apply to the formulation of commodity pools, Congress made clear that the new provision was not intended to impair the Commission's exclusive jurisdiction and that the states remain preempted in this area. S. Rep. No. 384, 97th Cong., 2d Sess. 81 (1982). H.R. Rep. No. 565 (Part 1), 97th Cong., 2d Sess. 82 (1982). Indeed, Chairman Helms noted that this Committee found it unnecessary to add a provision to the new Section 4m(2) which would have explicitly preempted all substantive state law because "existing law clearly preempt[s] the states from this area of regulation." 128 Cong. Rec. S13097 (Oct. 1, 1982).

The Commission previously expressed this view in a February 27, 1981 letter commenting on the then proposed NASAA guidelines. Most recently, the Commission again expressed this view in an August 5, 1983 comment letter to NASAA on pro-

posed amendments to its guidelines. Copies of the February 27, 1981 and August 5, 1983 letters are attached. NASAA adopted revised amendments in September, 1983.

If state regulation of pools were limited to pool operators which are not registered with the Commission as required, the NASAA guidelines would be consistent with the open season provisions of new Section 12(e) of the Act. However, the Commission feels it has an obligation to voice its objections to requirements such as the NASAA guidelines, since the Act preempts state regulation of commodity pool operators which conform their activities to the requirements of the Act.

COMMODITY FUTURES TRADING COMMISSION,
Washington, D.C., August 5, 1983.

Re Proposed North American Securities Administrators Association ("NASAA") Guidelines for Registration of Commodity Pool Programs.

NORTH AMERICAN SECURITIES ADMINISTRATORS ASSOCIATION,
c/o Mr. Lee Polson,
Deputy Securities Commissioner,
Texas Securities Board, Austin, Texas.

DEAR SIRS AND MADAMS: The Commodity Futures Trading Commission wishes to submit the following comments to NASAA on its 1983 proposed commodity pool guidelines. The Commission's view is that while States serve a vital role in the investigation and prosecution of commodity-related fraud and abuse, a role that was reemphasized and expanded by the Futures Trading Act of 1982,[1] States remain preempted from imposing regulatory requirements on commodity pool operators, such as those requirements proposed in the 1983 NASAA guidelines.[2]

As you know, during Congressional enactment of the Futures Trading Act of 1982 both NASAA and the Commission sought to develop workable and pragmatic approaches in combating commodity fraud. This effort included legislative proposals by NASAA, provisions contained in the Commission's own 1982 legislative package, as well as detailed negotiations among Commission staff, a representative of NASAA and the staff of the Senate Permanent Subcommittee on Investigations with a view toward further expanding State prosecutorial powers.

Guiding the Commission's effort was its belief that, given the scope of unlawful off-exchange commodity activities and the limited resources of the Commission's own enforcement arm, active participation by the States is essential if American consumers are to be effectively protected against fraud operations. The Commission is thus anxious, now that the Futures Trading Act of 1982 has been signed into law, to work with NASAA and other State law enforcement representatives toward the effective implementation of the new anti-fraud enforcement provisions.

Two provisions of the Futures Trading Act of 1982 hold particular promise in this regard: (i) the "open season" provision, which allows states to apply their own laws and regulations against persons who unlawfully engage in commodity transactions outside the Act's regulatory structure[3], and (ii) the increased sharing of prosecutorial information between the CFTC and the States.[4] Both of these proposals were supported by NASAA, and were substantially similar to amendments contained in NASAA's own 1982 legislative package.[5] The Commission is hopeful that State officials will increasingly employ these new legal tools in developing commodity-related anti-fraud cases, and we certainly stand prepared to offer our assistance in that effort.

Similarly, the Commission's Advisory Committee on State Jurisdiction and Responsibilities under the Commodity Exchange Act, which contains representation

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[1] Pub. L. No. 97-444, 96 Stat. 2294, 7 U.S.C.A. Section 2 et seq. (1983).

[2] The Commission previously commented in 1981 on similar guidelines proposed by NASAA and in 1977 on the Central Securities Administrators Council's proposed guidelines. *See* February 27, 1981 letter to NASAA from the Secretary of the Commission, which is attached. *See* also [1977-1980 Transfer Binder] Comm. Fut. L. Rep. (CCH) Paragraph 20,445 (July 5, 1977).

[3] Section 12(e) of the Commodity Exchange Act, as amended, 7 U.S.C.A. Section 16 (1983).

[4] Sections 8(e) and 8(g) of the Act, as amended, 7 U.S.C.A. Sections 12(e) and 12(g) (1983). The role of the States in enforcing federal law has also been expanded by the adoption of new Section 6d(8), 7 U.S.C.A. Section 13a-2(8) (1983), which permits States to bring actions in their own courts for fraudulent activities of commodity pool operators and other persons registered with the Commission which violate the Act or Commission regulations. *See* e.g., Section 4o of the Act, 7 U.S.C. Section 6o. States continue to have authority to bring civil actions in federal court for violations of the Act and Commission regulations and actions in state court for violations of any general civil or criminal State antifraud statutes. Section 6d of the Act, 7 U.S.C. Section 13a-2.

[5] *See* Hearings on S. 2109 Before the Subcommittee on Agricultural Research and General Legislation of the Senate Committee on Agriculture, Nutrition and Forestry, 97th Cong. 2d Sess. 632-633 (1982).

from both NASAA and the Commission, can be a useful forum for developing ideas to improve the effectiveness of these provisions. We would welcome the input of NASAA in preparing an agenda for the Advisory Committee's next upcoming meeting along these lines.

With regard to NASAA's proposed commodity pool guidelines, however, the Commission's view with respect to Federal pre-emption of these requirements remains unchanged. Section 2(a)(1) of the Commodity Exchange Act, 7 U.S.C. Section 2, as amended, vests in the Commission "exclusive jurisdiction . . . with respect to account, agreements . . . and transactions involving" futures, options and leverage contracts.

Since the Commission's beginning in 1974, Congress has stated its preference for a single, uniform national regulatory scheme for the commodity futures industry to avoid duplicative and potentially conflicting State and federal regulation. The House-Senate Conference Committee on the CFTC Act stated:

"Under the exclusive grant of jurisdiction to the Commission, the authority in the Commodity Exchange Act (and the regulations issued by the Commission) would preempt the field insofar as futures regulation is concerned. Therefore, if any substantive State law regulating futures trading was contrary to or inconsistent with Federal law, the Federal law would govern. In view of the broad grant of authority to the Commission to regulate the futures trading industry, the Conferees do not contemplate that there will be a need for any supplementary regulation by the States." S. Rep. No. 1194, 93d Cong. 2d Sess. 35–36 (1974).

Congress made commodity pool regulation one aspect of the Commission's "broad grant of authority." In 1974, Congress determined that the activities relating to commodity pools that trade futures contracts "are affected with a national public interest" since these transactions "occur in such volume as to affect substantially transactions on contract markets." Section 4*l* of the Act, 7 U.S.C. Section 6*l*. For this reason, Congress expressly subjected commodity pools and commodity pool operators, for the first time, to the comprehensive regulatory scheme of the Commodity Exchange Act.[6]

The legislative history of the Futures Trading Act of 1982 confirmed the Commission's exclusive jurisdiction over commodity pool activities. During its consideration of new Section 4m(2), 7 U.S.C.A. Section 6m(2), which clarifies the extent to which the federal securities laws apply to the formation of commodity pools, Congress made clear that the new provision "is not intended to impair the exclusive jurisdiction of the CFTC over the operations of a commodity pool in connection with its trading of futures contracts. . . ." H.R. Rep. No. 565 (Part 1), 97th Cong., 2d Sess. 82 (1982). The House Committee on Agriculture plainly stated with respect to this provision: "Registration or regulation of commodity pools under any other Federal securities statutes or under any State securities or 'Blue Sky' laws is preempted." Id. at 83. Indeed, the Senate Committee on Agriculture, Nutrition, and Forestry found it unnecessary to add a provision to the new Section 4m(2) which would have explicitly preempted all substantive State law because "existing law clearly preempt[s] the states from this area of regulation." 128 Cong. Rec. S13097 (Oct. 1, 1982) (Statement of Chairman Helms). Accordingly, under the Act, "the several states are specifically preempted from the substantive regulation or qualification of commodity pools and commodity pool operators." S. Rep. No. 384, 97th Cong., 2d Sess. 81 (1982).[7]

If the proposed NASAA guidelines were limited to pools which are not registered with the Commission or which deal in commodity transactions outside the Act's regulatory structure, such as "off-exchange" futures contracts, the guidelines would be consistent with new Section 12(e). However, as currently written, the Commission feels it has an obligation to voice its objections, since the Act clearly preempts State

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[6] *See* Sections 2(a)(1), 4*l*, 4m, 4n and 4*o* of the Act, 7 U.S.C. Sections 2, 6*l*, 6m, 6n and 6*o*. *See* also Section 8a(5) of the Act, 7 U.S.C. Section 12(a)(5). Under this authority, the Commission has developed a regulatory scheme governing commodity pools and commodity pool operators. *See* 17 C.F.R. Part 4 (1982).

[7] In adopting new Section 6d(8), the Commission's exclusive jurisdiction again was noted by the House-Senate Conference Committee:

The conferees intend that nothing contained in this provision will permit any State to impose, or to initiate any suit, action, or proceeding for an alleged violation of, any State licensing, registration, or qualification requirement provided for under any State securities or commodities statute. Similarly, nothing in this provision permits any State to initiate any suit, action, or proceeding against a person registered under the Act for an alleged violation of any rule, regulation, guideline, or statement of general policy issued under any State securities or commodities statute.

H.R. Rep. No. 964, 97th Cong., 2d Sess. 43 (1982).

regulation of those commodity pools and commodity pool operators which conform their activities to the requirements of the Act.

The Commission's efforts during the 1982 reauthorization process, such as its support of the "Roth-Rudman" amendment,[6] were based on the Commission's firm belief that the States must play a vigorous role in combating customer abuse in commodity related transactions. The Commission welcomes the opportunity for more extensive State involvement in actions against those who engage in unlawful conduct under a "commodity" theme and pledges its support to the States, particularly as they exercise their new authority granted under the Futures Trading Act of 1982.

Sincerely,

JANE K. STUCKEY,
Secretary of the Commission.

COMMODITY FUTURES TRADING COMMISSION,
Washington, D.C., February 27, 1981.

Re Proposed North American Securities Administrators Association, ("NASA") Guidelines for Registration of Commodity Pool Programs.

NORTH AMERICAN SECURITIES ADMINISTRATORS ASSOCIATION,
c/o Mr. Jamie A. Wade,
NASAA Subcommittee Chairman, Securities Division,
Lucas State Office Building, Des Moines, Iowa.

DEAR SIRS: The Commodity Futures Trading Commission is pleased to have this opportunity to submit these comments to NASAA on its proposed commodity pool guidelines. The Commission is an independent, federal regulatory agency created in 1974 to administer and enforce the provisions of the Commodity Exchange Act ("Act"), 7 U.S.C. Section 1 et seq. (1976 and Supp. III 1979). The Act provides a "comprehensive regulatory structure to oversee the volatile and esoteric futures trading complex." H.R. Rep. No. 975, 93d Cong., 2d Sess. 1 (1974). As part of this structure, the Act authorizes the Commission to regulate the broad spectrum of activities related to commodity pools and commodity pool operators.[1] Under this authority, the Commission has developed a regulatory scheme governing commodity pools and commodity pool operators. *See* 17 C.F.R. Part 4 (1980). Thus, the Commission has a significant interest in the proposed NASAA guidelines, which provide for regulation of commodity pools and commodity pool operators under State law.

These proposed guidelines amend, and generally make more stringent, the guidelines for commodity pools and commodity pool operators that have previously been adopted by the Central Securities Administrators Council ("CSAC").[2] If adopted, these proposed guidelines will likely have a substantial impact upon commodity pools and commodity pool operators in this country.[3]

Accordingly, the Commission's Advisory Committee on State Jurisdiction and Responsibilities held a public hearing on these guidelines on December 4, 1980. As recommended by the Advisory Committee, we are providing you with a copy of the full record of its deliberations. The record consists of a transcript of the public hearing, written submissions received by the Advisory Committee from members of the public and the written statements of certain members of the Advisory Committee.

As you will see, the predominant theme of the members of the public that appeared before the Advisory Committee was that customer abuses have not occurred

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[6] The "Roth-Rudman" amendment, which was rejected by the House-Senate Conference Committee, would have permitted State officials to bring actions in State courts for violations of State antifraud provisions. *See* 128 Cong. Rec. S13084 (Oct. 1, 1982).

[1] *See* Sections 2(a)(1), 4*l*, 4m, 4n, and 4*o* of the Act, 7 U.S.C. §§ 2, 6*l* 6m, 6n, and 6o. *See* also Section 8a(5) of the Act, 7 U.S.C. Section 12(a)(5).

[2] The Commission's staff submitted comments on the CSAC guidelines when they were proposed. In a letter to John R. Larson, Commissioner of Securities for the State of Minnesota, Commission staff expressed the view that these proposed guidelines were preempted by the Act and Commission regulations. *See* [1977-80 Transfer Binder] Comm. Fut. L. Rep. (CCH) Section 20,445 (July 5, 1977). In that letter, the Dupty General Counsel of the Commission stated:

"We note that several aspects of the Council's proposed guidelines appear to regulate the activities of commodity pool operators. We believe, however, that the states have been preempted from imposing regulatory requirements on commodity pool operators, through adoption of the Council's guidelines or otherwise." Id. (footnote omitted).

[3] For example, the proposed NASAA guidelines would impose restrictions with respect to brokerage commissions which the pool may be charged, mandate more restrictive limitations on management and incentive fees concerning the pool's operation and prohibit the pool from entering into new positions in the futures markets if margin commitments of the pool exceed two-thirds of the net assets in the pool.

with respect to commodity pools in such magnitude as to warrant the new stringent requirements contained in the proposed guidelines. Moreover, many witnesses also explained that the proposed guidelines would, in many instances, conflict with regulatory judgments previously made by this Commission. And, some individuals expressed the view that the States were preempted from adopting the proposed guidelines by virtue of the grant of exclusive regulatory jurisdiction to this Commission in Section 2(a)(1) of the Act, 7 U.S.C. Section 2.

On February 5, 1981, the Advisory Committee concluded its deliberations on the proposed NASAA guidelines. The Committee recommended, by a vote of 5 to 3, that the Commission should formally advise NASAA "of the Commission's legal position that, in contrast to State laws of general applicability, State statutes, regulations or guidelines purporting to regulate activities involving commodity pools and commodity pool operators are preempted by the Commodity Exchange Act and the United States Constitution."

The Commission has now determined to adopt this recommendation of its Advisory Committee. Section 2(a)(1) of the Act, 7 U.S.C. section 2, vests in the Commission "exclusive jurisdiction with respect to accounts, agreements . . . , and transactions involving" future contracts. In our view, the full range of activities related to commodity pools, including the solicitation of prospective participants in the pool as well as the pool's management and operation, fall within this grant of exclusive regulatory authority to the Commission.

Moreover, when Congress enacted this exclusive jurisdiction provision in 1974, Congress made plain that the Commission's exclusive jurisdiction applies to all phases of a commodity pool. In 1974, Congress determined that the activities relating to commodity pools that trade futures contracts "are affected with a national public interest" since these transactions "occur in such volume as to affect substantially transactions on contract markets." Section 4*l* of the Act, 7 U.S.C. section 6*l*. For this reason, Congress expressly subjected commodity pools and commodity pool operators, for the first time, to the comprehensive regulatory scheme of the Commodity Exchange Act. *See* supra n. 1. Commodity pool regulation is, therefore, one aspect of "the broad grant of authority to the Commission to regulate the futures trading industry" which Congress mandated in 1974 would "preempt the field insofar as futures regulation is concerned." S. Rep. No. 1194, 93d Cong., 2d Sess. 35-36 (1974) (Report of the Committee of Conference). Indeed, the Commission's exclusive authority was of such magnitude that Congress did "not contemplate that there will be a need for any supplementary regulation by the States." Id. at 36. Accordingly, Congress has preempted the States from adopting or enforcing either the proposed NASAA guidelines or the existing CSAC guidelines.[4]

By adopting this position, the Commission is not seeking to extend its statutory authority in any way. In our view, no other result is consistent with the Commission's statutory mandate and Congress' purposes in enacting the exclusive jurisdiction provision in Section 2(a)(1) of the Act.

This does not mean, however, that the States should not have an important role in connection with the Commission's adoption of uniform regulatory standards governing commodity pools and pool operators. The Commission will give serious consideration to the views of the States in connection with the Commission's ongoing rulemaking proceeding involving proposed changes to its commodity pool regulations. *See* 45 Fed. Reg. 51600 (Aug. 4, 1980). For this purpose, the Commission will consider the proposed NASAA guidelines as public comments on the Commission's proposed rules. In addition, the Commission would greatly appreciate receiving from NASAA, or its member States, any information documenting abuses or other problems in the formation or operation of commodity pools. In this regard, the Commission would be interested in receiving a copy of the public comments NASAA has received concerning its proposed guidelines.

The Commission firmly believes, and wishes to reiterate, that the States must play a vigorous role in combating customer abuses in commodity-related transactions. The Commission and the States share the common goal of protecting the public from fraudulent and otherwise unlawful conduct. To this end, the Commission pledges to continue to cooperate fully with the States in instituting enforcement actions under and otherwise fully effectuating Section 6d of the Commodity Exchange Act, 7 U.S.C. section 13a-2 (Supp. III 1979), and will assist and cooperate with the States, in any way possible, to make Section 6d an effective means for supplementing the Commission's enforcement program.

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[4] The Commission will, in the near future, publish in the Federal Register a formal interpretation of its exclusive jurisdiction with regard to commodity pools under the Act. This interpretative statement will describe in greater length the legal bases for the Commission's position.

The Commission, like State law enforcement and regulatory agencies, has limited resources available for discharging its obligations to the public. We would, therefore, not attempt to assert jurisdiction over activities where our authority is of doubtful validity. We would assume that State officials adhere to a similar policy and, therefore, will not adopt or enforce commodity pool regulations under State law. The Commission looks forward to continued cooperation with the States.

Very truly yours,

JANE K. STUCKEY,
Secretary of the Commission.

INTRODUCING BROKERS

Question. As you know, one of the principal objectives of the 1982 reauthorization legislation was the registration and regulation of agents of futures commission merchants as introducing brokers. The Commission recently adopted final rules to implement the provisions of the 1982 Act concerning introducing brokers. What are some of the difficulties the Commission encountered in formulating a regulatory program in this area?

Answer. In seeking to formulate a comprehensive regulatory framework for introducing brokers and the other new categories of registrant, the primary difficulty confronting the Commission was the general uncertainty within the futures industry as to how previously unregistered persons intended to continue their businesses after adoption of the new regulations. In particular, there was a split between futures commission merchants ("FCMs") who wished to perform only clearing functions for those "agents" which referred customer business to them and futures commission merchants who wished to use such "agents" as exclusive sales representatives and to take full responsibility for their sales practices. Another problem was that the former agents ranged in size from large securities wirehouses to small "mom and pop" operations. The Commission endeavored to develop a regulatory program for introducing brokers which recognized these differences and was responsive to them.

During the rulemaking process, the most consistent comment received opposed the proposed net capital requirements. The effective net capital requirement as proposed was $37,500. In its final rules, the Commission reduced the independent capital requirement to $20,000 and adopted an alternative capital requirement which provides that an introducing broker need not maintain its own capital if it is operating pursuant to a guarantee agreement with an FCM under which an FCM which carries accounts for the introducing broker's customers will assume regulatory and financial responsibility for the activities of the introducing broker. Such an introducing broker also has no financial reporting requirements. The Commission believes that the approach of the final rules provides affected persons with the maximum flexibility as to their manner and form of operation and will effectuate to Congressional purpose that introducing brokers have a sufficient reserve of capital to remain economically viable yet not be so onerous as to constitute a barrier to the entry into, or continuation in, the commodities industry.

Question. Do you think that the rule package will need to be modified in the future to reflect experience with how the regulations work out in practice?

Answer. As a general matter, the Commission regularly reviews its regulations to make technical changes based upon the changing nature of the futures industry. With respect to the adoption of a regulatory framework to govern the activities of introducing brokers and the associated persons of introducing brokers, commodity pool operators and commodity trading advisors, the Commission recognizes that experience may demonstrate that some minor changes in the regulations are required. However, I do not believe that significant revisions will be necessary, since substantial efforts were made to solicit and consider the views of affected parties during the rulemaking process. For example, the Commission's staff held open meetings in New York and Chicago both prior and subsequent to the adoption of final rules. The presentations were well-attended and provided a useful forum for the Commission's staff to answer specific questions, to provide further guidance to affected persons and to be advised as to the nature of any practical problems being experienced during the implementation of the rules. In addition, the Commission received over 100 comment letters on its initial rulemaking proposal which provided valuable assistance to the Commission's staff in preparing regulations which are responsive to the function, purposes and size of the entities being regulated. The Commission believes that the final rules reflect its consideration of the concerns of the affected persons and the generally good response to the final rules thus far seems to indicate

that the Commission's regulatory framework for introducing brokers constitutes an appropriate balance between customer protection and regulatory requirements.

Of course, the Commission will continue to monitor the effect of these rules and will consider such revisions to the system which has been adopted as may be appropriate. In particular, the Commission will closely monitor the impact of the alternative capital requirements. In this regard, it should be noted that as of October 31, 1983, approximately 294 introducing brokers out of a total 591 former agents have elected to use the alternative net capital requirement and have entered into a guarantee agreement with an FCM. The Commission intends to monitor vigorously the use of such guarantee agreements to ensure that the alternative provided by the Commission is not abused.

Question. Have the backlogs regarding the processing of registration applications submitted by introducing brokers as well as other categories of registrant been eliminated?

Answer. There is currently no registration backlog with respect to the processing of registration applications for introducing brokers by the National Futures Association ("NFA"). When the Commission published its final rules to govern introducing brokers and the other new categories of registrant created by the Futures Trading Act of 1982, the Commission also published a notice in the Federal Register containing a list of the former agents of FCMs which the NFA had determined were clearly qualified for the Commission's "no-action" position regarding introducing brokers. 48 Fed. Reg. 35305 (August 3, 1983). Thus, the new registration rules did not adversely affect or interrupt the ongoing businesses of such agents. In its August 3, 1983 notice, the Commission also reminded those persons whose names appeared on the list compiled by the NFA that the Commission's "no-action" position would terminate automatically if an applicant for registration as an introducing broker failed to achieve and demonstrate compliance with the minimum financial requirements for introducing brokers by October 31, 1983. Thus, the Commission granted those agents intending to become introducing brokers approximately ninety days from the publication date to comply with the minimum financial requirements.

As of today, the Commission has determined that out of a total of 591 former agents deemed eligible by the NFA for the Commission's "no-action" position, 495 have attempted to comply with the Commission's minimum capital requirement. Those firms which have met the October 31, 1983 deadline or requested an extension of time have been permitted to remain in business. Of course, new applicants for registration as an introducing broker are required to submit a registration application to the NFA and must be granted registration prior to the initiation of business. This is consistent with the treatment afforded to all new applicants for registration, whether applications are filed with the Commission or NFA. These applications are being processed by the NFA in due course.

With respect to other categories of registrant, the Commission has achieved significant progress in eliminating the backlog in registration applications while at the same time implementing regulations requiring the registration of the new categories of registrant created by the Futures Trading Act of 1982. For example, the Commission granted 48,000 registrations in fiscal year 1983, a 50% increase over fiscal year 1982. Because of the implementation of a fingerprinting requirement for all new registrants, the amount of paperwork to be processed by the Commission's staff has increased dramatically. Moreover, the Commission has allotted fewer resources for registration processing as a result of the anticipated transfer of this function to the NFA which, at the present time, is not expected to be complete until the end of fiscal year 1984.

The processing of registration applications has also been hampered by the high number of registration applications which are submitted in deficient form. Although it is the applicant's responsibility to file a complete application with the Commission, forty percent of all applications are deficient in some way. (Similarly, ninety-seven percent of all applications submitted to the NFA pursuant to the Commission's "no-action" position have been deficient.) As a result, the time to process all applications is increased. Commission staff has discussed this problem with industry representatives and are working together to resolve this problem. The Commission has also proposed rules which would permit the granting of temporary licenses consistent with the Commission's authority as established by the Futures Trading Act of 1982.

THE NATIONAL FUTURES ASSOCIATION

Question. What is your assessment of NFA's operations to date?

Answer. The Commission believes that the National Futures Association ("NFA") is moving forward in a number of important areas. In the year since NFA commenced its operations, it has adopted and obtained Commission approval of all rules needed to comply with section 17(p) of the Act. More important, NFA now has in place a broad ranging surveillance and compliance program which includes annual limited scope financial audits of all non-exchange FCM members, biannual full scope financial and sales practice audits of all non-exchange FCM members, ongoing surveillance of non-exchange FCM members' capital situation, and financial audits of commodity pool operator and commodity trading advisor members. In March 1983 NFA also began to regulate and audit the options activities of its member FCMs. As introducing brokers ("IBs") become members of NFA, they, too, will be included in NFA's broad auditing progam. Moreover NFA's Business Conduct Committee meets monthly to review staff investigations and related matters and to take appropriate disciplinary action. By the end of October, NFA has issued 9 complaints and 10 warning letters and taken 8 member responsibility actions and 2 disciplinary actions.

NFA has also instituted its arbitration program for the resolution of claims and disputes by customers against NFA members. By the beginning of November 1983, NFA had received a total of 83 Intents to Arbitrate, from which 38 Demands for Arbitration actually were filed. Six cases have been settled, five cases have already proceeded to hearing and awards have been issued and several other cases are ready to proceed.

In the spring of 1983 NFA also started to assume some of the Commission's registration functions by taking on the administration of the Commission's "no action" position for introducing brokers and their associated persons ("APs"). That initial function was followed by the transfer of authority to grant registration to applicants in those two registration categories in August 1983, when the Commission's final rules governing IBs and APs of IBs were adopted. NFA is continuing to enhance its registration program and has indicated that it will seek Commission authorization to perform additional registration functions. The Commission anticipates that NFA will be prepared to assume all Commission registration functions in late fiscal year 1984 or early fiscal year 1985.

Question. The CFTC has taken steps to ensure coordination of its own activities with those of the National Futures Association. What further steps need to be taken?

Answer. The Commission currently ensures coordination of activities with the National Futures Association ("NFA") in a number of ways. First, the Commission reviews NFA rules and related proposals before implementation as required by the Act. In addition, the Commission maintains more informal contact with NFA through monthly status reports which NFA provides to describe its progress in developing and administering its programs. Not only has the Commission staff briefed the Commission periodically on NFA's progress, but NFA has also appeared before the Commission at open public meetings on two occasions to discuss their programs and respond to questions.

Morever, the Commission has established frequent communication and discussion between its own and NFA's staff. In addition to routine matters, the Commission and NFA share audit scheduling information and regularly exchange information concerning potential enforcement matters. In a related effort, NFA has designated a liaison with the states and has begun to coordinate appropriate matters directly with them.

In addition to coordination of such regulatory activities, the Commission and NFA also share registration information, as NFA begins to assume responsibility for registration functions as authorized by the Commission. In that regard, the Commission is working with NFA to assume that the Commission has available to it appropriate means to access the computerized registration data bank that NFA will maintain.

Question. Do you see any areas in which the allocation of resources by the CFTC may be reduced or readjusted to reflect NFA's activities? In this regard, do you anticipate that the gradual assumption by NFA of additional CFTC functions will result in significant changes in what the CFTC will be doing down the road?

Answer. NFA obtained its registration from the Commission in September 1981, but did not commence formal operations until October 1, 1982. Its immediate impact on the Commission's budgetary requirements has been nominal, with routine Commission auditing of the limited number of non-exchange member FCMs being replaced by the financial audit and review procedures of NFA. The limited Commission resources which this NFA function have freed for other tasks has readily been absorbed in the Division of Trading and Markets' oversight audits, enforcement sup-

port and in direct auditing of commodity pool operators ("CPO") and commodity trading advisors ("CTAs").

Similarly, NFA has just begun to assume its registration responsibilities under the authorization of the Commission. Through the spring and early summer of this year, NFA was authorized by the Commission to process applicants for Commission registration in the new categories of introducing broker and associated persons of introducing brokers. More recently, the Commission authorized NFA to grant applications for registration in these two categories. The assumption of these registration functions—which apply to new categories of registrant created by the 1982 reauthorization legislation—has not yet had any impact upon the Commission's need to devote resources to its registration responsibilities. NFA has, however, discussed with Commission staff its tentative plans for assuming responsibility for additional categories of Commission registrant during fiscal year 1984. At this point, it appears that NFA will not be prepared to be authorized to register the largest category of Commission registrants—associated persons of FCMs—until the end of fiscal year or the beginning of fiscal year 1985. Accordingly, the Commission will be unable to reallocate or reduce its resources to reflect NFA's registration of associated persons until the first quarter of fiscal year 1985 at the earliest.

While the Commission's registration progam and its financial monitoring of non-exchange member FCMs previously have involved the dedication of Commission resources, the other regulatory functions which NFA will be assuming have not involved a previous commitment of significant Commission resources. For example, the addition of NFA personnel to the self-regulatory framework existing within the commodities industry will mark the first time that either the Commission or the industry have devoted significant resources to monitoring industry-wide sales practices, to proficiency testing and to the routine and comprehensive monitoring of CPOs and CTAs.

As NFA assumes further responsibilities in the sales practice and CPO/CTA areas, the Commission should be able to make some further adjustments in the use of its staff resources. While NFA's initial efforts to audit non-exchange member FCMs has permitted the Division of Trading and Markets to direct its auditing staff to devote greater resources to self-regulatory organization oversight audits and to direct Commission auditing of those CPOs and CTAs which are not yet fully covered by NFA, NFA's eventual assumption of comprehensive auditing responsibility for the CPO and CTA membership categories (as well as the new category of introducing brokers) should free Commission audit resources to provide comprehensive auditing oversight of NFA and the exchanges to assure that their direct audits of member firms are conducted in an adequate manner. In addition, the Commission's auditing resources will be redirected to provide greater support for enforcement, investigatory and litigation matters. Finally, as the number of diverse contracts traded and overall trading volume continue to grow, Commission auditing staff may be used to bolster the Commission's market surveillance and trade practice surveillance program.

In summary, the Commission anticipates that the presence of a comprehensive self-regulatory organization will supplement the Commission's regulatory objectives. Initially, NFA will be performing functions in those areas where the Commission has lacked adequate resources to assure comprehensive regulatory oversight, such as auditing non-exchange member FCMs. As NFA expands, some reordering of Commission resources in the registration and direct auditing areas will occur in recognition of NFA's assumption of responsibilities in those areas. These changes will cause the Commission's direct regulatory activities as Congress intended. Accordingly, Commission staff will be used primarily to provide oversight of NFA's and the exchanges' auditing functions, to provide the Division of Enforcement with greater auditing and trade practice investigatory support, and to supplement NFA's direct auditing responsibilities at firms (FCMs, CPOs, or CTAs) where particular concerns are identified.

NEW CONTRACTS

Question. Do you have any difficulty in reconciling your inclination that the market should be left to decide the merits of a particular contract with the CFTC's present interpretation of the statutory requirement for contract market designation, that is, each contract must serve an economic purpose as a hedging vehicle or as a price discovery mechanism? Do you think the answer may be that the traditional tests of economic purpose need to be reexamined in light of the development of all these new contracts?

Answer. I believe that the Commission's current designation procedures leave considerable latitude for the market testing of new contracts. The Commission's guideline requires that a board of trade demonstrate that a new contract can reasonably be expected to be used for price basing or the hedging of price risks on more than an occasional basis. Such a demonstration must of course be prospective, subject generally to the considerations that there is a potential pricing or hedging use for the contract and that the terms are in conformity with a significant segment of the underlying cash market. These are, incidently the major factors which CFTC also reviews in determining that a new contract is not unduly susceptible to manipulation or other forms of market disruption.

Our experience has been that these designation requirements fulfill the Commission's mandate to preserve orderly trading and protect the public interest while leaving considerable latitude to the exchanges in the area of new product innovation and contract design. Since the institution of this guideline in 1975, for instance, the Commission has designated a number of new contracts in the area of financial instruments including both public and private interest bearing securities and stock market indices. The concept of cash settlement has been incorporated into some of these contracts. Moreover, in many instances competing exchanges have been approved to trade contracts which are generically the same but which have dissimilar terms. For instance the recently approved Chicago Board of Trade and New York Mercantile Exchange crude oil contracts are based on different cash markets.

The Commission has no assurance, of course, and makes no effort to guarantee that each new contract will succeed, or which set of contract terms is commercially the most acceptable. These are matters which are routinely left to the market place.

Question. What progress has been made in reducing the time necessary for processing contract market designation applications? What further steps need to be taken to expedite the process?

Answer. In late 1980 the Commission instituted a number of steps to increase the rate at which new designations could be considered with existing staff resources. These included a total reorganization and geographic consolidation of its market analysis personnel in the Washington, D.C. office, and revisions in the manner in which contract reviews were processed and forwarded to the Commission. In September 1981, the Commission instituted a new policy concerning voluntary withdrawal of designations by contract markets which failed to respond to Commission requests for additional information concerning the submission within ninety days. Finally, in November 1982, the Commission published revisions to guidelines for the preparation of exchange submissions for the purpose of clarifying and updating the requirements. As a result of these steps the Commission has been able to process over 54 designation applications since January 1981, compared to only 29 in the prior five and one-half years. Despite this accomplishment, the relative processing time for new applications has not dropped significantly since during this time period the exchanges continued to submit new contracts at a very high rate.

Recent amendments to the Commodity Exchange Act and Commission regulations may alter the current situation substantially. The 1982 amendments to the Act provide that the Commission has a one-year period to designate a contract or institute disapproval proceedings, but this one year period is extended by the time the exchange takes to respond to Commission requests on material deficiencies in the initial application. This amendment, by placing a cap on the time allowed for Commission action provides a concrete incentive for timely complete responses from exchanges concerning application deficiencies. In addition, by this mandatory twelve month time period, the individual exchanges are encouraged to consider their own priorities and resources more carefully in submitting contracts.

In addition, the Commission recently instituted service fees for processing designation applications, effective September 23, 1983, for previously submitted as well as newly submitted applications. The purpose of this fee was to recover the cost of the government's services in processing designation applications. An additional consequence was that on or before the effective date the exchanges withdrew 28, or over one half of the designation applications then pending with the Commission. It is too early, however, fully to assess the overall effect of the statutory amendments and institution of the service fee on the processing time for new applications.

Question. Do you see any special difficulties in designating several commodity exchanges to trade the same or very similar contracts? Does trading of the same or similar contracts by multiple commodity exchanges pose any particular problems for the CFTC in ensuring market integrity? In this connection, are you concerned about the proliferation of similar contracts from the standpoint of a possible lowering of standards in order to attract business or do you feel it stimulated innovation and creativity?

Answer. The experience with identical or similar futures contracts indicates that the trading activity generally, tends to focus on one market. In addition, once an active viable market is established in a commodity, the chances of successfully introducing a second related contract are reduced. In view of this it appears that the designation of similar or identical contracts is not harmful, and may be beneficial. First, since the contract replication process does not appear to expand overall trading volume or open interest, it does not increase the demand for the underlying commodity for purposes of delivery. Replication does, however, provide a means for exchanges to compete positively in the area of contract design since it appears that a better designed contract would be needed for success. In fact, experience indicates that the threat of successful introduction of a similar contract encourages exchanges to keep their contracts up-to-date and consistent with current commercial practices. On the other hand, the designation process and general Commission oversight of the contract market guarantees that the competition between exchanges will not lower the standards of contract design or acceptable standards of conduct.

RELATIONS WITH THE SEC

Question. What steps has the CFTC taken, during your tenure on the Commission, to improve coordination and consultation with the SEC on matters of mutual concern? Do you see a need for further improvements in any areas?

Answer. Since I joined the Commission in November 1981, several important steps have been taken to improve our relationships with the Securities and Exchange Commission, both in terms of sharing market information as well as developing better coordination and consultation on issues of mutual concern:

In December 1981, the CFTC and SEC concluded an accord which clarified our respective jurisdictions over financial-based options and futures contracts, including those based on stock market indices. Our two agencies worked together closely during Congressional enactment of this accord in 1982;

The implementation of the 1982 accord has involved the CFTC and SEC in a continuous working relationship. The CFTC has regularly consulted with the SEC before acting to designate proposed stock-index futures or options-on-futures contracts. In addition, SEC and CFTC staffs have met regularly to share surveillance data regarding these actively traded markets;

During the past year, the CFTC and SEC worked together on several joint study projects involving financial trading markets, including:

The Task Group on Regulation of Financial Services, chaired by Vice President George Bush, which has reviewed a range of financial issues including the Federal regulation of futures and options markets. The Task Group includes the Chairmen of both the CFTC and the SEC, and both agencies have participated extensively in the development of data and recommendations;

The Federal Reserve Board has led a major study of the futures industry, mandated by the Futures Trading Act of 1982. Again, both the CFTC and SEC have participated extensively in this project;

The Federal Reserve has also initiated a study on margin rules in both futures and securities, including staff coordination with the SEC and CFTC.

Each of these studies has provided a forum for the SEC and CFTC to discuss and debate outstanding regulatory issues, and to develop common approaches to issues of mutual concern;

CFTC and SEC have worked to eliminate unnecessary differences in our regulations where appropriate, particularly where divergent rules have been burdensome to participants in both the securities and futures markets. Rules have been harmonized involving reporting and net capital requirements. Last May, the CFTC and SEC solicited public comments on how best to proceed in this effort.

The current level of CFTC-SEC communication and cooperation is strong in my opinion, and I intend to work hard to maintain this effective relationship.

Question. Could you give me your perspective on how the CFTC's jurisdictional accord with the SEC has worked to date?

Answer. The CFTC and SEC have worked successfully with the jurisdictional accord. As you know, the Johnson-Shad agreement negotiated between the two agencies was announced jointly on December 7, 1981, and later embodied in the futures Trading Act of 1982, which became effective on January 11, 1983. (P.L. 97-444, 96 Stat. 2294 (1983)). From December 1981 to January 1983, the CFTC transmitted to the SEC for comment 5 applications for designation as a contract market, all of which the SEC agreed should be approved. Since January 1983, nine applications for designation as a contract market have been transmitted to the SEC for comment. Of these, the SEC has agreed that two be approved, and comments on the remaining

seven are forthcoming. Representatives of the two agencies continue to meet to formulate guidelines for implementing the standards set by the accord.

In the spirit of cooperation between the two agencies, the CFTC has also transmitted recently to the SEC for comment several applications for designaton as a contract market that are not subject to the accord but may be of interest to the SEC, such as option contracts on foreign currency. Comments on these applications are also expected shortly.

Question. Do you believe that the issues between the two agencies that were not definitively resolved by the enactment of the accord should be addressed by further legislation or should the two agencies be left to work them out?

Answer. Because the CFTC and SEC are working successfully with the accord, I do not believe that further legislation is needed at the present time. In this connection, I believe that any new legislative proposal should await completion of the study of the futures industry being conducted by the Federal Reserve Board, the CFTC, the SEC, and the Treasury Department. As you know, that study is to be completed by September 30, 1984. Of course, should issues arise prior to that time that the CFTC and SEC are unable to resolve jointly through the regulatory process, we would recommend appropriate legislation.

Question. The CFTC, along with the SEC, is a participating agency in Vice President Bush's Task Group on Regulation of Financial Services. Would you tell me about the CFTC's contribution to the work of this group and your assessment of its progress to date?

Answer. The Task Group on Regulation of Financial Services, under the leadership of Vice President Bush and Treasury Secretary Regan, has provided an important public forum for the airing of many important and sometimes controversial issue in the financial arena, including the respective roles of the CFTC and the SEC in regulating the trading of financial-based futures and options contracts. I have welcomed this public scrutiny and debate, and I believe that its outcome will be beneficial to all concerned.

Like all member agencies, the CFTC's participation in the Bush Task Group has been extensive. Last April, the CFTC prepared a comprehensive Report to the Task Group commenting on a wide range of regulatory issues and reform proposals, and discussed steps that have been taken to improve our regulatory coordination with the SEC. CFTC staff members have spent many hours working in each of the six subcommittees assigned by the Task Group to develop recommendations in different areas, as well as the overall "working group" which is responsible for compiling final staff proposals for consideration by the Task Group principals.

I expect the Task Group members themselves will meet in the near future to discuss these staff proposals, and present our final recommendations to President Reagan.

Question. Do you believe that serious disparities exist between regulation of similar entities and products by the CFTC under the Commodity Exchange Act and by the SEC under the federal securities laws? If so, what should be done about them to eliminate any unfair competitive advantages resulting from such disparities?

Answer. As a result of continuous dialogue between the CFTC and SEC, the two agencies have already eliminated or, in some situations, greatly reduced disparities in the regulation of similar entities and products. In this vein, the CFTC and SEC recently published requests for public comment on ways to further streamline regulations that may be duplicative or overlapping for industry professionals registered with both agencies. Representatives of the CFTC and SEC have met to discuss the comments received and to plan appropriate inter-agency cooperative efforts.

In addition, the CFTC and SEC have taken steps to identify and resolve perceived regulatory disparities that may be interpreted to affect competing products on their merits. Of course, not all regulatory disparity necessarily generates competitive advantage or disadvantage. For example, both SEC-regulated stock index options and CFTC-regulated stock index futures have enjoyed success.

Particularly with respect to new products, their success or failure may depend substantially upon factors such as marketing, product design, producer reputation, and channels of distribution. As exchanges compete for attention with innovative marketing programs, futures commission merchants (and securities brokers) may be well-advised to make their concerns known at the exchange level.

As you are aware, the comprehensive study of the futures industry pursuant to the Future Trading Act of 1982 is designed to address many of the issues in this area.

COMMODITY FRAUDS

Question. There have been a number of stories in the media recently about commodity frauds involving the sale of precious metals. It is reported that unsuspecting customers may lose millions of dollars due to the "boiler room" activities of unscrupulous bullion dealers.

Of course, I understand that the Commission generally doesn't have jurisdiction over non-futures transactions. Nontheless, these activities threaten to harm the reputation of others in the commodities industry.

What will the Commission be doing, during your term as Chairman, to help clean up this mess?

Answer. The Commodity Exchange Act, 7 U.S.C. § 1, et seq. (1983), provides the Commission with authority over "contracts of sale of a commodity for future delivery" (commodity futures contracts), as well as commodity options and leverage transactions. However, as you correctly noted, the Commission's jurisdiction is limited. The Act specifically states "[t]he term 'future delivery' . . . shall not include any sale of any cash commodity for deferred shipment or delivery" (so-called forward contracts). 7 U.S.C. § 2. Nor does the Commission have regulatory jurisdiction over cash commodity transactions.

During the past year, several precious metals dealers—the International Gold Bullion Exchange, United Precious Metals and Bullion Reserve of North America—have failed. Based on the information our staff has received, it is my understanding that each of these firms was engaged in either cash or deferred delivery transactions outside the Commission's regulatory jurisdiction.

The Commission plans to continue to refer information it receives on firms offering precious metals for immediate or deferred delivery to state enforcement officials and to appropriate federal agencies for their consideration. Also, the Commission has begun to make a special effort to make states aware of the opportunities available to them to prosecute firms engaged in fraudulent activities with a commodity theme, both under the Act's "open season" provision and otherwise. In October 1983, the Commission conducted a two-day cooperative enforcement seminar at which representatives from 20 states were present, which specifically included discussions about commodity frauds involving the sale of precious metals. The Commission plans scheduling additional cooperative enforcement seminars.

The Commission also plans to use its Advisory Committee on State Jurisdiction and Responsibilities Under the Commodity Exchange Act as a forum for developing ideas on how the Commission might better assist states in combatting commodity frauds involving cash sales of precious metals. And the Commission currently is assisting both the Subcommittee on Commerce, Consumer and Monetary Affairs of the House Committee on Government Operations and the Permanent Subcommittee on Investigations of the Senate Committee on Governmental Affairs, which are investigating the recent failures of the three precious metals dealers mentioned above.

BIOGRAPHICAL RÉSUMÉ—WILLIAM E. SEALE, MARCH 24, 1983

Home: 1936 Franklin Avenue, McLean,Virginia, (703) 241-8866.

Marital Status: Married, 2 sons (ages 19 and 18), 1 daughter (age 15).

Born: Lynchburg, Virginia, February 10, 1941.

Education: A.B.—Chemistry, University of Kentucky, 1963; M.S.—Agricultural Economics, University of Kentucky, 1969, Areas of Specialization: Production Economics, Farm Management; Ph. D.—Agricultural Economics, University of Kentucky, 1975, Areas of Specialization: Production Economics, Agriculture Policy.

Experience

May 1979-March 1983—Vice President—Government Relations, Commodity Exchange, Inc; New York, New York.

Duties: Monitored and analyzed all legislative and regulatory activities that may have impacted Comex—the worlds largest metal futures exchange—or the futures industry; managed a 5 person staff, represented the exchange to federal legislative and regulatory bodies; assisted in formulating comprehensive strategy to deal with government related matters; developed and conducted educational programs about futures trading; assisted in exchange policy development regarding a wide variety of futures related issues.

March 1975-May 1979—Legislative Assistant to United States Senator Walter D. Huddleston.

Duties: Development of agriculture, consumer and commodity related legislation; conferring with individuals and groups with respect to problems and/or pending or

proposed legislation; extensive public speaking regarding legislative issues; key role in development and enactment of the Futures Trading Act of 1978—the first reauthorization of the Commodity Futures Trading Commission as well as other major legislation; active in dealing with domestic and international agriculture and economic problems; coordinating legislative activities of the Senate Subcommittee on Agricultural Production, Marketing and Stabilization of Prices.

January 1970–February 1975—Department of Agricultural Economics, University of Kentucky.

Duties: Operating a subscription farm management/farm analysis program for commerical grain farmers; classroom teaching; production economics research; organizing and teaching farm management schools for farm operators; consultations regarding financial and estate planning; teaching short courses for producers regarding the hedging uses of futures markets.

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OFFICE OF GOVERNMENT ETHICS,
OFFICE OF PERSONNEL MANAGEMENT,
Washington, D.C., November 7, 1983.

Hon. JESSE A. HELMS,
Chairman, Committee on Agriculture, Nutrition, and Forestry,
U.S., Senate, Washington, D.C.

DEAR MR. CHAIRMAN: In accordance with the Ethics in Government Act of 1978, I enclose a copy of the financial disclosure report filed by William E. Seale, who has been nominated by President Reagan for the positio of Commissioner, Commodity Futures Trading Commission.[1]

We have reviewed the report and have also obtained advice from the Commodity Futures Trading Commission concerning any possible conflict in light of the Commission's functions and the nominee's proposed duties. Based thereon, we believe

[1] The financial discloures report has been retained in the committee files.

that Mr. Seale is in compliance with applicable laws and regulations governing conflicts of interest.

Sincerely,

DAVID H. MARTIN, *Director.*

STATEMENT OF HON. DANIEL OLIVER-GENERAL COUNSEL-DESIGNATE U.S. DEPARTMENT OF AGRICULTURE

Mr. Chairman, members of the Committee, it is a great honor for me to appear before this Committee as the President's nominee for the office of the General Counsel of the Department of Agriculture.

As you may know, I have served since the beginning of this Administration as the General Counsel of the Department of Education. Prior to that, my professional life consisted essentially of practicing law in New York City, and writing for and helping to edit a small, but preeminent, national journal of politics and the arts. I lived in Connecticut, which, I note in passing—and passing very quickly—produced five and a half million pounds of tobacco in 1981, whereas North Carolina produced only 800 million pounds.

It would be a great honor for me to serve the President and the Secretary of Agriculture, as General Counsel of the Department of Agriculture and I appear before you today to seek your consent and the consent of the Senate to my nomination.

The office of the General Counsel is not primarily a policy-making office: instead, it responds to the initiative of others, whether they are inside the Department bringing policy changes, or outside bringing lawsuits.

You might be interested to know that, according to a memo I received yesterday, in the five years since October of 1978, the number of cases the Office of the General Counsel has on its books has gone up from 11,000 to 31,000. During the month of October, 1978, attorneys completed work on 8,400 items; this year they completed work on 13,000 items. The backlog in October of 1978 was 6,300 uncompleted items; this year it was 16,000 items.

Notwithstanding that increase in the workload, the staff has grown only from 207 attorneys then to 227 attorneys now.

One of my jobs as General Counsel of the Department of Agriculture will have to be to determine how well the Office is coping, and what can be done if it is not coping adequately.

Mr. Chairman, I will be happy to try to respond to any questions you may have.

BIOGRAPHY OF DANIEL OLIVER, GENERAL COUNSEL-DESIGNATE, U.S. DEPARTMENT OF AGRICULTURE

Daniel Oliver, 44, started his active political career working in William F. Buckley, Jr.'s campaign for Mayor of New York City in 1965. He also ran for the New York State Assembly that year, as well as in the following year, and again in 1968. In 1970 he was Director of Research for James L. Buckley's New York senatorial campaign. In 1971 he served as Editorial Assistant at National Review magazine, and as Special Assistant to the Editor, William F. Buckley, Jr. From 1973 to 1976 he was the Executive Editor of National Review.

He also practiced law in New York for almost a decade, first with the firm of Hawkins, Delafield & Wood, and subsequently with Alexander & Green. During the years 1959–62 he served in the U.S. Army as a Russian Language Specialist.

A 1964 graduate of Harvard College, Mr. Oliver received his LL. B. degree from Fordham University Law School and was admitted to the New York Bar in 1967. He has served as a Director of National Review, Inc., The American Conservative Union, Inc., the New York State Political Action Committee, the Society for the Preservation of the Book of Common Prayer, and the National Association of Concerned Parents and Educators. Mr. Oliver is a Trustee-elect of the Philadelphia Society.

Mr. Oliver is also a former Vestryman of Christ (Episcopal) Church, Greenwich, Connecticut. He is married to the former Louise Vietor of New Haven. They have five children—Louisa, Andrew, Daniel, Susan, and Peter.

He has served as President Reagan's General Counsel at the Department of Education since August 5, 1981.

OFFICE OF GOVERNMENT ETHICS,
OFFICE OF PERSONNEL MANAGEMENT,
Washington, D.C., November 7, 1983.

Hon. JESSE A. HELMS,
Chairman, Committee on Agriculture, Nutrition, and Forestry,
U.S. Senate, Washington, D.C.

DEAR MR. CHAIRMAN: In accordance with the Ethics in Government Act of 1978, I enclose a copy of the financial disclosure report filed by Daniel Oliver, who has been nominated by President Reagan for the position of General Counsel, Department of Agriculture.[1]

We have reviewed the report and have also obtained advice from the Department of Agriculture concerning any possible conflict in light of the Department's functions and the nominee's proposed duties. Mr. Oliver has detailed the assets of certain family trusts and custodial accounts, in several of which he and his wife enjoy contingent beneficial interests. Further, he and his wife serve as trustees and his wife serves as a custodian on certain trusts established for the benefit of his five dependent children. Neither Mr. Oliver or his wife enjoy a direct beneficial interest in these trusts. Mr. Oliver has resigned as trustee of the trusts established under the instruments of his late father and his mother.

John R. Block, Secretary of Agriculture, has issued (within his wide latitude under the statute to do so) an anticipatory waiver under subsection (b)(1) of 18 U.S.C. § 208 of the applicability of section 208(a) because in his opinion the assets of the trusts and accounts are sufficiently diversified and Mr. Oliver's own beneficial interests sufficiently contingent and remote to be "not so substantial as to be likely to affect the integrity of the services which the Government may expect." Otherwise, that statute would operate to impose liability on Mr. Oliver for participation in matters arising within the Department involving corporations whose securities are held by the trusts and accounts in question.

Mr. Oliver has also sold certain of his securities interests in order that no actual or apparent conflict of interest exist. Finally, since Mr. Oliver and his wife and children own interests in a number of corporations involved either directly or indirectly in coal mining operations, Mr. Oliver has agreed to perform no functions under the Surface Mining Control and Reclamation Act during his tenure as General Counsel.

Mr. Oliver's letter of November 2, 1983 detailing his interests and pledging the steps referred to above, and a copy of Secretary Block's letter to Mr. Oliver waiving the provisions of 18 U.S.C. § 208(a) with respect to interests held by the described family trusts and accounts, are enclosed with this letter.

Based thereon, we believe that Mr. Oliver is in compliance with applicable laws and regulations governing conflicts of interest.

Sincerely,

DAVID H. MARTIN, *Director.*

DEPARTMENT OF AGRICULTURE,
OFFICE OF THE SECRETARY,
Washington, D.C., November 2, 1983.

Hon. DAVID H. MARTIN,
Director, Office of Government Ethics, Office of Personnel Management, Washington, D.C.

DEAR MR. MARTIN: Enclosed is the SF 278, Financial Disclosure Report, filed by Daniel Oliver in connection with his nomination to be General Counsel of the Department of Agriculture, which I have signed as this Department's Designated Agency Official. Since 1981, Mr. Oliver has been employed as General Counsel of the Department of Education.

Mr. Oliver has made full disclosure of his own personal financial interests and those of his spouse and dependent children. He has likewise detailed the assets of certain family trusts and custodial accounts, in several of which he and his wife enjoy contingent beneficial interests, and in certain of which—those established for the benefit of his five dependent children—he and his wife serve as trustees, and his wife as a custodian, but they enjoy no direct beneficial interest. Mr. Oliver has resigned as trustee of the trusts established under the instruments of his late father and his mother. Because Mr. Oliver and his wife and children do enjoy beneficial interests in the assets of these family trusts and custodial accounts, there is a potential that matters may arise within the Department involving one or more of the corporations whose securities are held among their assets, and a potential as well that

[1] The financial disclosure report has been retained in the committee files.

Mr. Oliver's participation in any such matters could constitute a violation of 18 U.S.C. 208. Because the assets of the trusts and accounts are so widely diversified, however, and because Mr. Oliver's own beneficial interests therein are so contingent and remote, Secretary of Agriculture John R. Block has issued a waiver under subsection (b) of 18 U.S.C. 208, from the applicability of section 208(a) as that section might otherwise operate to impose liability on Mr. Oliver for participation in matters arising within the Department involving corporations whose securities are held by the trusts and accounts in question.

Mr. Oliver has also sold certain of his securities interests in order that no actual or apparent conflict of interest exist. Finally, since Mr. Oliver and his wife and children own interests in a number of corporations involved either directly or indirectly in coal mining operations Mr. Oliver has agreed to perform no function under the Surface Mining Control and Reclamation Act during his tenure as General Counsel of this Department.

On the basis of the information contained in Mr. Oliver's Financial Disclosure Report, and considering both the waiver issued by the Secretary regarding Mr. Oliver's interests and those of his children in the several family trusts and accounts, and the additional steps which Mr. Oliver has agreed to take in connection with his nomination to be General Counsel of this Department, I have concluded that his appointment to that position will pose no actual or apparent conflict of interest under applicable laws and regulations. Mr. Oliver's letter to you detailing his interests and pledging the steps referred to above, and a copy of the Secretary's letter to Mr. Oliver waiving the provisions of 18 U.S.C. 208(a) with respect to interests held by the described family trusts and accounts, are enclosed with this letter.

Sincerely,

WILLIAM J. RILEY, JR.,
Director of Personnel and Designated Agency Official.

Enclosures.

WASHINGTON, D.C., *November 2, 1983.*

The Honorable DAVID H. MARTIN,
Director, Office of Government Ethics, Office of Personnel Management, Washington, D.C.

DEAR MR. MARTIN: The purpose of this letter is to outline the steps which I have taken, and those which I intend to take, in order to assure that no actual or apparent conflict of interest will arise between my personal financial interests and the duties which I will perform as General Counsel of the Department of Agriculture.

I have served until recently as trustee in connection with trusts established under instruments of my late father, Andrew Oliver, and my mother, Ruth B. Oliver. While I have resigned my positions as trustee of those trusts, I do retain a limited and contingent financial interest in the assets of each. I currently receive no income or other direct or indirect benefit under either trust, and my interest in each can best be described as that of a contingent remainderman or a contingent income beneficiary. The same is true of another trust established under the instrument of my grandfather, W. H. P. Oliver, under which my only interest is that of contingent remainderman; and of a trust established by A. G. B. Vietor for the benefit of my wife, under which I serve as a trustee but enjoy no beneficial interest.

All of the trusts which I have described hold interests in a number of corporations and organizations which do business with the Department of Agriculture, are regulated by the Department, or are affected in a substantial way by the Department's program and operations. Since the securities held as part of the assets of each of these trusts are so widely diversified, however, and since my beneficial interest in the assets of each such trust is so contingent and remote, it has been concluded that this is an appropriate case for use of a waiver under subsection (b) of 18 U.S.C. 208. Since there is a possibility that matters may arise during my tenure as General Counsel of the Department of Agriculture, affecting one or more of the corporations and organizations whose securities are held as part of the assets of the described trusts, the possibility likewise exists that my participation in any such matter would give rise to a conflict of interest such as those proscribed by 18 U.S.C. 208. In these circumstances, Secretary of Agriculture John R. Block has determined that my contingent beneficial interests in the trusts in question are "not so substantial as to be likely to affect the integrity of the services which the Government may expect" from me. Under subsection (b) of section 208, Secretary Block has thus issued a waiver from the applicability of section 208(a), as that section might otherwise operate to impose liability on me for participation in matters arising within the Department and involving the corporations and organizations whose securities are held by

the trusts in question. A copy of Secretary Block's letter to me containing such waiver is enclosed.

Separate trusts have also been established for the benefit of my five dependent children. Mrs. Oliver and I serve jointly as trustees of those trusts, which are irrevocable in nature, but we do not now nor will we in the future enjoy any beneficial interests under any of them. Likewise, custodial accounts have been established for the benefit of our five children; my wife serves as custodian of those accounts, but neither my wife nor I enjoy any beneficial ownership interest therein. Our dependent children are the principal beneficiaries of these trusts and accounts, and their interests in the trusts will vest when they cease to be minors. Like the trusts described above, these trusts and accounts likewise own interests in corporations and organizations whose activities are affected by the programs and operations of the Department of Agriculture, and the potential exists here as well that matters will arise within the Department during my tenure involving one or more of the corporations and organizations whose securities are held as part of the assets of one or more of these trusts and accounts. The assets of these trusts and accounts are likewise diversified, however, and my wife and I enjoy no direct beneficial interest therein. Here too, therefore, it has been deemed appropriate that a waiver be granted under 18 U.S.C. 208(b), and Secretary Block's letter applies to the assets of these trusts and accounts as well.

My Financial Disclosure Statement also reflects ownership by my wife and me, either separately or jointly, of securities interests in two firms whose operations are regulated or affected by the programs and activities of the Department of Agriculture. I have directed that our joint holdings in those firms, Inco Ltd. (operations include metals and mining, oil and gas, genetic engineering) and Glaxo Holdings (pharmaceuticals, veterinary products, food and medical equipment), be sold in order that no actual or apparent conflict of interest exist.

One other issue requires addressing. My wife, my dependent children, and I own, either separately, jointly, or as part of the assets of one or more of the trusts and custodial accounts described above, interests in a number of corporations involved directly or indirectly in coal mining operations. The Surface Mining Control and Reclamation Act provides, in section 201(f) [30 U.S.C. 1211(f)], that no Federal employee performing any function or duty under that Act may own any direct or indirect financial interest in surface or underground coal mining operations. While principal responsibility for administration of the Act resides with the Secretary of the Interior, the Department of Agriculture also performs certain functions under the Act and the General Counsel's position is among those which have been designated for this purpose. While most of the interests in corporations involved in any way in coal mining operations are held among the assets of the trusts and custodial accounts described above, and only a few are held directly by my wife and myself, the clear language of the Act suggests that I should perform no functions thereunder while enjoying any ownership interest, however remote, in corporations engaged in coal mining operations. Therefore, during my tenure as General Counsel of the Department of Agriculture, I will perform no function under that Act. Any matter which may arise under that Act during my tenure—whether involving statutory interpretation, policy formulation, or a matter of a particular nature involving specific outside parties—will be handled by the Deputy General Counsel and other members of the staff of the Office of the General Counsel.

I believe that I have made full disclosure of my personal financial interests and those of my wife and minor children. I believe as well that, in light of (1) my resignations as trustee of the trusts established under the instruments of Andrew Oliver and Ruth B. Oliver; (2) the waiver issued by the Secretary of Agriculture under 18 U.S.C. 208(b) with respect to ownership interests held by the several trusts and custodial accounts described earlier in this letter; and (3) my commitment to abstain from performance of any functions under the Surface Mining Control and Reclamation Act, no actual or apparent conflict of interest will arise between my personal financial interests on the one hand, and the duties I will perform as General Counsel of the Department of Agriculture on the other.

Sincerely,

DANIEL OLIVER.

Attachment.

DEPARTMENT OF AGRICULTURE,
OFFICE OF THE SECRETARY,
Washington, D.C., November 1, 1983.

DANIEL OLIVER, Esq.,
Washington, D.C.

DEAR MR. OLIVER: Through your Financial Disclosure Report (SF-278), you have provided information regarding certain financial interests held by you and other members of your family, including ownership of a widely diversified securities portfolio. In addition to securities held in your name and that of your wife, and in the name of your wife as custodian for your minor children, you have reported as well a wide range of stock interests held by a number of family trusts, including trusts established by your late father, Andrew Oliver, by your mother, Ruth B. Oliver, by your grandfather, W. H. P. Oliver, and separate trusts and custodial accounts established for the benefit of your five dependent children.

Among the securities interest held as part of the corpus of each of the described trusts, there are a number of securities issued by corporations which must be considered to constitute "interested parties" in terms of the programs and operations of this Department because in some of their operations they have contracts or other direct business relationships with this Department, operations which are regulated under programs administered by this Department, or business activities which are directly affected by the programs and operations of this Department. The securities owned by the trusts in question are numerous and diversified, and it is unnecessary to detail in this letter either the names of the corporations whose securities are included, the extents to which such securities are held under any of the trust instruments, or the relationships between the business activities of any such corporations and the programs of the Department of Agriculture.

I conclude that, were all of such interests held directly by you or your spouse or minor children, a clear potential would exist for a conflict of interest to occur such as those barred by the provisions of 18 U.S.C. 208. Your interests, however, in the trusts established by your late father, by your mother, and by your grandfather, are remote. It is my understanding that you currently receive no income under any of these trusts, and that your only interest in any of the trusts may fairly be described as that of either a contingent remainderman or a contingent income beneficiary—i.e., that you will receive no benefit under the terms of any of these three trusts until some unspecified future date.

Different circumstances exist with respect to the separate trusts and the custodial accounts established for the benefit of your five dependent children. It is my understanding that here too, while you and Mrs. Oliver serve as trustees of the trusts, and Mrs. Oliver as custodian of the accounts, your children are the principal beneficiaries of both. I understand that the trusts are irrevocable in nature, and that your children's interests thereunder will vest when they cease to be minors. I understand as well that you and Mrs. Oliver enjoy no direct beneficial ownership interest in the trusts' assets or those of the custodial accounts.

Also for consideration is the trust established for the benefit of your wife, under which you serve as trustee with A. G. B. Vietor. It is my understanding that you enjoy no beneficial interest in the assets of that trust. While your wife is the principal beneficiary, it too has assets which are widely diversified.

Since the trusts established under the instruments of Andrew Oliver, Ruth B. Oliver, and W. H. P. Oliver present circumstances in which you hold interests thereunder, however contingent and remote, in corporations and entities whose business operations are affected by the programs and activities of the Department of Agriculture, I conclude there is a potential that matters will arise in the course of your performance of official duties as General Counsel of this Department, involving corporations whose securities are held as part of the trusts in question, and that your participation in such matters could constitute a violation of the provisions of 18 U.S.C. 208. The same is true with respect to the trusts established for the benefit of your wife and children and with respect to your children's custodial accounts; that is, there is a potential that matters will arise within the Department during your tenure involving corporations whose securities are held among the assets of these trusts and accounts, and your participation in such matters could likewise constitute a violation of 18 U.S.C. 208. Pursuant to Executive Order 11222, delegating to me the authority in section 208(b)(1), I am authorized to grant a waiver from the applicability of section 208(a) if it is determined that your private interest in decisions affecting those organizations whose securities are held by the described trusts and accounts "is not so substantial as to be deemed likely to affect the integrity of the services which the Government may expect" from you.

Because your personal interests in any of the trusts and accounts in question are so remote, and because the holdings of the trusts are so diversified, I do not believe that these interests are likely to influence you in your discussions or decisions of matters arising within the Department of Agriculture. Accordingly, I hereby grant you a waiver from the applicability of section 208(a), as that section might otherwise operate to impose liability on you for your participation in matters arising within the Department relating to the corporations and organizations whose securities are held by the trusts and accounts in question.

Sincerely,

JOHN R. BLOCK,
Secretary of Agriculture.

U.S. HOUSE OF REPRESENTATIVES,
COMMITTEE ON AGRICULTURE,
SUBCOMMITTEE ON CONSERVATION, CREDIT, AND RURAL DEVELOPMENT,
Washington, D.C., November 8, 1983.

The Honorable JESSE HELMS,
Chairman, Senate Committee on Agriculture, Nutrition, and Forestry,
Washington, D.C.

DEAR MR. CHAIRMAN: In advance of your committee conducting a hearing on the nomination of Dr. Susan Meredith Phillips to be Chairman of the Commodity Futures Trading Commission, we wish to offer our full endorsement and support for this Presidential nomination.

As Chairman and Ranking Minority Member of the House Agriculture Subcommittee on Conservation, Credit and Rural Development, which has responsibility in the oversight of the Commodity Futures Trading Commission, we are well acquainted with Dr. Phillips and her record in academia as well as her record as Commissioner of the CFTC from November 1981 to May 1983, and as Acting Chairman from May 1983 to the present. Needless to say, it is a most impressive history. Her list of accomplishments in the research and study of options and futures trading speaks for itself, testifying to her commitment to the financial market place.

Dr. Phillips possesses the technical knowledge and thorough understanding of the futures markets, its various participants, and the industry's needs for progress that are so important for the effective performance of a chairman of this agency. Her consummate skill in these areas and in management are of benefit to the CFTC as it changes with the rapidly expanding futures industry.

During Dr. Phillips' stewardship as Acting Chairman, we have been impressed by her energy in implementing various provisions of the Futures Trading Act of 1982, and her responsiveness to requests by this Subcommittee. In all, the relationship between this Subcommittee and the Commission under her leadership is perhaps the best we have seen to date.

It is for these reasons that we believe Susan Phillips to be an outstanding choice for Chairman of the CFTC. With the greatest of confidence, we recommend her to the Committee.

Sincerely,

ED JONES, *Chairman.*
E. THOMAS COLEMAN,
Ranking Minority Member.

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